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TRANSCRIPT OF RECORD

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, ~~1929~~ 1930

No. ~~741~~ 61

DAVID BURNEE

ROBERT H. LUCAS, COMMISSIONER OF INTERNAL REVENUE, PETITIONER

vs.

NIAGARA FALLS BREWING COMPANY AND PAUL A. SCHOELLKOPF, CHARLES E. HAEBERLE, ET AL., ETC.

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

PETITION FOR CERTIORARI FILED MARCH 15, 1930
CERTIORARI GRANTED APRIL 28, 1930

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1929

No. 741

ROBERT H. LUCAS, COMMISSIONER OF INTERNAL REVENUE PETITIONER

vs.

NIAGARA FALLS BREWING COMPANY AND PAUL A. SCHOELLKOPF, CHARLES E. HAEBERLE, ET AL., ETC.

ON PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

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1 In United States Circuit Court of Appeals for the Second Circuit

NIAGARA FALLS BREWING COMPANY, PAUL A. SCHOELLKOPF, CHARLES E. HAEBERLE, FRED H. KRULL, EDSON, P. PFOHL, ALBERT E. MAYLE, and GEORGE F. NYE, as Surviving Directors of said Company and Trustees Thereof in Dissolution, appellants

against

ROBERT H. LUCAS, COMMISSIONER OF INTERNAL REVENUE OF THE Treasury Department of the United States, appellee

Statement under rule 13

This proceeding was commenced by the filing of a petition for appeal with the United States Board of Tax Appeals on the 10th day of October, 1925.

The original parties to this proceeding were Niagara Falls Brewing Company and Paul A. Schoellkopf, Charles E. Haeberle, Fred H. Krull, Edson P. Pfohl, Albert E. Mayle, George F. Nye, Frederick Chormann, and Rudolf V. Rose, as directors of said company and trustees thereof in dissolution. Said Frederick Chormann and Rudolf V. Rose have died pending this appeal, and this proceeding is continued by the other directors of said company as survivors.

2 The defendant's answer was filed on the 3rd day of November, 1925.

The amended complaint was filed on the 14th day of December, 1925.

The answer to the amended complaint was filed on the 21st day of January, 1926.

The trial was had before honorable Charles M. Trammell on the 12th day of May, 1927.

There has been no arrest herein, or attachment of property: no question was referred to a commisioner, master, or referee.

The interlocutory decree herein was entered October 16, 1928.

The final decree herein was entered January 18, 1929.

This appeal was taken June 24, 1929.

3 Before United States Board of Tax Appeals

APPEAL OF NIAGARA FALLS BREWING COMPANY, 732 THIRD Street, Niagara Falls, New York, and Paul A. Schoellkopf, Charles E. Haeberle, Fred H. Krull, Edson P. Pfohl, Albert T. Mayle, Frederick Chormann, Rudolf V. Rose, and George F. Nye, as Directors of said Company and Trustees Thereof in Dissolution

Petition

Filed Oct. 10, 1925

The above-named taxpayer and the above-named individuals as directors of said taxpayer and trustees thereof in dissolution, pur-

suant to section 35 of the general corporation law of the State of New York, do hereby jointly and severally appeal from the determination of the Commissioner of Internal Revenue set forth in his deficiency letter under symbols IT:CA:2227–6, dated August 13, 1925, and as the basis of this appeal set forth the following:

1. The taxpayer was organized and incorporated under and by virtue of the laws of the State of New York, February 26, 1902, and has its principal office and place of business at Niagara Falls, New York. Under and pursuant to sections 220 and 221 of the general corporation law of the State of New York (now section 105 of the stock corporation law of the State of New
4 York), said taxpayer corporation was duly dissolved upon voluntary consent of the stockholders thereof by certificate duly filed in the office of the Secretary of State of the State of New York, December 1, 1921, as appears by the certificate of the second deputy secretary of state of the State of New York duly issued on said date.

2. The deficiency computed by the collector was assessed against the taxpayer under the provisions of section 274 (d) of the revenue act of 1924 and was set forth in a letter dated November 26, 1924, copy of which letter is hereto annexed, marked "Schedule A," and made a part of this petition.

Thereafter and about January 1, 1925, notices and demand for said taxes shown by Schedule A were received by the taxpayer, copies of which notices and demand are hereto annexed, marked "Schedule B," and made a part of this petition.

Said notices and demand were accompanied by a letter dated January 5, 1925, from the collector of internal revenue, Buffalo, New York, under symbols 3199–CJP, copy of which letter is annexed to this petition, marked "Schedule C," and made a part hereof.

On January 15, 1925, the taxpayer duly filed its claim for abatement of said asessments, pursuant to the terms of said letter, Schedule A, copy of which claim for abatement is hereto annexed, marked "Schedule D," and made a part of this petition.

Upon filing said claim for abatement said taxpayer filed a bond by demand of the said collector, copy of which bond is hereto annexed, marked "Schedule E," and made a part of this petition.

Thereafter and on or about August 15, 1925, the taxpayer received a letter from the Commissioner of Internal Revenue, dated August 13, 1925, copy of which is hereto annexed, marked "Schedule F," and made a part of this petition, denying said claim for abatement.

5 3. The taxes in controversy are income and excess-profits taxes for the calendar years 1918 and 1919 and are more than $10,000, to wit, the sum of $25,988.70.

4. The deficiency of tax asserted in said assessment of November 26, 1924, Schedule A, and said notices and demand, Schedule B, said claim for abatement, Schedule D, and said letter of August 13, 1925, Schedule F, is based upon the following errors:

(a) Said assessments are contrary to the revenue act of 1918 and the acts amendatory thereof and supplemental thereto and the regulations of the Treasury Department promulgated in pursuance thereof, in that the said assessments fail to allow to the taxpayer as deductions from its gross income in computing its net income—"a reasonable allowance for the exhaustion wear and tear of property used in the trade or business of the taxpayer, including a reasonable allowance for obsolescence."

(b) Said assessments are contrary to the revenue act of 1918 and the acts amendatory thereof and supplemental thereto and the regulations of the Treasury Department promulgated in pursuance thereof, in that the said assessments fail to allow to the taxpayer as deductions from its gross income in computing its net income—"losses sustained during the taxable year and not compensated for by insurance or otherwise incurred in the trade or business of the taxpayer."

5. The facts upon which the taxpayer relies as the basis of its appeal are as follows:

(a) The taxpayer was organized for the purpose of producing, distributing, and selling malt and spirituous liquors. For
6 that purpose it purchased the buildings at 732 Third Street, Niagara Falls, New York, and built other buildings and purchased and installed machinery, fixtures, and equipment. Said buildings, machinery, fixtures, and equipment were devoted solely to that purpose (and to a minor extent to the purpose of making and selling soft drinks) until the taxpayer discontinued the business of brewing and distilling malt and spirituous liquors, as hereinafter set forth.

(b) The said buildings, machinery, fixtures, and equipment of the taxpayer were acquired by it for the most part prior to March 1, 1913. The fair market value of said buildings, machinery, fixtures, and equipment on March 1, 1913, was as follows:

Real estate, brewery:		Signs	375.00
Land	$100,000.00	Saloon furn. and fixt	15,890.54
Buildings (stone)	148,192.18	Small cooperage	2,576.50
Machinery	60,658.35		362,840.31
Casks and tanks	20,974.46	Outside property [redacted]	38,128.55
Horses, wagons, etc	8,039.63		400,968.86
Office furn. and fixt	1,936.65		
Auto trucks	4,197.00		

Said value was determined as the sound value of the said property as of December 24, 1912, by the American Appraisal Company, of Milwaukee, Wisconsin, and no factors to substantially increase or reduce the value between December 24, 1912, and March 1, 1913, were present or occurred.

7 (c) Said soft-drink department, machinery, and equipment were acquired by the taxpayer after March 1, 1913, and were of the cost of $4,533.09. On or about December 18, 1917, the Congress of the United States adopted a resolution for the amend-

ment of the Constitution of the United States, which, so far as is material, is as follows:

"After one year from the ratification of this article the manufacture, sale, or transportation of intoxicating liquors within, the importation thereof into, or the exportation thereof from the United States and all territory subject to the jurisdiction thereof for beverage purposes is hereby prohibited."

and submitted the same to the various States for ratification.

(d) On January 31, 1918, the ratification of said amendment by the several States had so far proceeded as to clearly indicate ultimate ratification thereof by the requisite number of States.

(e) On January 29, 1919, the requisite number of States had ratified said amendment, as appears by the certificate of ratification thereof by the Acting Secretary of State of the United States issued under said date.

(f) On November 21, 1918, the President of the United States signed and made effective chapter 212 of the Statutes of the United States for 1918, being chapter 212, volume 40, Statutes at Large, page 146, which made it unlawful to sell for beverage purposes any distilled spirits and made it unlawful to use grain, cereal, fruit, or other food products in the manufacture or production of beer, wine, or other intoxicating malt or vinous liquors for beverage purposes, or to sell such beer, wine, or other intoxicating malt or vinous liquors.

(g) On August 10, 1917, the President of the United States
8 signed and made effective an act of Congress of the United States known as chapter 53, section 15, of the Statutes of 1917, set forth at 40 Statutes at Large, page 282, as part of the national defense act, which provides:

"Whenever the President shall find that limitation, regulation, or prohibition of the use of foods, fruits, food materials, or feeds in the production of malt or vinous liquors for beverage purposes, or that reduction of the alcoholic content of any such malt or vinous liquor, is essential, in order to assure an adequate and continuous supply of food, or that the national security and defense will be subserved thereby, he is authorized, from time to time, to prescribe and give public notice of the extent of the limitation, regulation, prohibition, or reduction so necessitated. Whenever such notice shall have been given and shall remain unrevoked no person shall, after a reasonable time prescribed in such notice, use any foods, fruits, food materials, or feeds in the production of malt or vinous liquors, or import any such liquors except under license issued by the President and in compliance with rules and regulations determined by him governing the production and importation of such liquors and the alcoholic content thereof. * * *"

Under and by virtue of said act the President of the United States by proclamation dated December 8, 1918, prohibited the production in the United States of any malt liquors except ale or porter

containing more than 2¾% of alcohol by weight; and further, by a proclamation of the President of the United States dated December 16, 1918, it was provided that—

9 "No person shall use any sugar, glucose, corn, rice or any other foods, fruits, food materials or feed, including malt, in the production of malt liquors, including near beer, for beverage purposes, whether or not such malt liquors contain alcohol";

and thereafter the said President of the United States by proclamation dated January 30, 1919, modified said last-named proclamation to permit the use of grain in the manufacture of beverages which are not intoxicating.

(h) On October 28, 1919, the President of the United States signed and made effective chapter 85 of the Statutes of the United States for 1919, being Title II thereof, set forth at 41 Statutes at Large, page 307, which provided that no person should manufacture, sell, deliver, or furnish any intoxicating liquors after the date when the said constitutional amendment of the United States went into effect, to wit, January 29, 1920, including any beer, ale, porter, wine, or any spirituous wine, malt, or fermented liquors containing one-half of one per cent or more of alcohol by volume and fit for beverage purposes.

(i) That the products manufactured by your petitioner prior to the promulgation of said eighteenth amendment to the Constitution of the United States and the adoption of said acts were intoxicating malt liquors containing more than one-half of one per cent of alcohol by volume; that the business and good will of your petitioner, as hereinafter described, were built up on the manufacture and sale of such beverages.

(j) That the officers, agents, and employees of your petitioner were continually aware of the adoption of said statutes and the proposal of said constitutional amendment and the progress of the adoption thereof.

10 (k) That during the calendar year 1918 the officers of your petitioner caused to be computed and written off on the books of your petitioner an extraordinary depreciation and allowance for obsolescence of the property of your petitioner due to the adoption, promulgation, and enforcement of said constitutional amendment and said statutes. Said obsolescence allowance was made in good faith and in the course of taxpayer's business and was due wholly and made solely because of the said legislation and constitutional amendment and is computed as follows:

Buildings (stone)	$27,014.33	Saloon furn. and fixt	$552.01
Machinery	45,606.41	Improvements	13,823.81
Casks and tanks	16,912.87	Small cooperage	2,132.71
Horses, wagons, etc	1,268.56		
Office furn. and fixt	532.42		110,047.52
Auto trucks	2,204.40		

(l) That during the calendar year 1919 the officers and directors of your petitioner caused to be computed and written off on the books

of your petitioner an extraordinary depreciation and allowance for obsolescence of the property of your petitioner due to the adoption, promulgation, and enforcement of said constitutinal amendment and said statutes. Said obsolescence allowance was made in good faith and in the course of taxpayer's business and was due wholly and made solely because of the said legislation and constitutional amendment and is computed as follows:

11	Buildings (stone)	$40,000.00
	Machinery	10,000.00
	Casks and tanks	928.48
	Office furn. and fixt	114.24
	Saloon furn. and fixt	450.00
		51,492.72

(m) That at the annual meeting of the board of directors of the taxpayer held February 5, 1919, the board of directors of taxpayer adopted a resolution as follows:

"Whereas the accounting department of this company has after due consideration and consultation with the officers of the company, and with its counsel, made up an operating statement for the year 1918, in which charges have been made for extraordinary depreciation to that part of the plant of this company which has been acquired for and is peculiarly adapted to the use in the brewing of malt liquors, because of actual as well as obvious and impending conditions tending to render such portions of the plant of greatly decreased value, because of conditions arising during said year 1918; and

"Whereas this board has duly considered the charges to operation so made, as shown by the report submitted on this date:

"Now, THEREFORE, BE IT RESOLVED, That the action of the accounting officers in making such charges to operations for depreciation of the tangible property of this company, occurring through actual as well as obvious and impending conditions relating to the business of the company for the year 1918, be and the same is in all things ratified and approved, and the accounting department is
12 hereby instructed permanently to enter such charges for extraordinary depreciation for the year 1918, amounting to $110,147.52, as tentatively proposed, upon the operating statement submitted to this board."

(n) That prior to the incidence, promulgation, enforcement, and adoption of said constitutional amendment and statutes the taxpayer had been engaged in, and the property on which obsolescence is claimed was entirely devoted to, the manufacture of spirituous and malt liquor, which manufacture was in the years 1918 and 1919 prohibited and forbidden by such constitutional amendment and statutes to the end that the taxpayer was obliged to give up and gave up the business of manufacturing such spirituous and malt liquor or beer with its said plant, machinery, equipment, and buildings.

(o) That the machinery, buildings, works, and equipment of the taxpayer so devoted to such manufacture of spirituous and malt liquor which was prohibited by said statutes and constitutional amendment, were especially designed and adapted for the purpose and are not available or practicable for use in that business or in any other business.

(p) That the said plant, machinery, equipment, works, and buildings of the taxpayer can not readily be used for any other purpose than that for which they were originally designed and specially adapted, as aforesaid, which use has been prohibited by the incidence, promulgation, enforcement, and adoption of said statutes and constitutional amendment.

(q) That the taxpayer, through its board of directors, officers, and agents, has leased said buildings, machinery, plant, and equipment, fixtures and furnishings, together with other buildings, machinery, works, furniture, fixtures, and equipment (upon which no
13 obsolescence deduction was taken upon the books of the taxpayer, but which were used in the production and sale of soft drinks) in good faith and at the highest available rate for a rental of $5,000 a year, plus taxes, insurance, and repairs, which was the highest rental offered to the officers and agents of the taxpayer for such buildings, machinery, works, equipment, furniture, and fixtures. Said rental capitalized in accordance with standard practice indicates a realizable value of $50,000 upon said machinery, buildings, works, equipment, furniture, and fixtures.

(r) The term of said lease is from January 15, 1922, to April 15, 1922. Said lease has renewed itself from time to time for periods of three months by operation of law and is at present outstanding and in force. No more favorable opportunity to lease said premises and no opportunity to sell the same, except as hereinafter set forth, has been presented to the officers and directors and agents of the taxpayer.

(s) That your taxpayer has in good faith endeavored to sell the property but has not been able to secure and has not received a higher offer than $50,000 for the said premises, and this offer was made by Mr. Walter Uptegraff, the president of Defiance Paper Company and Niagara Wall Paper Company, whose premises adjoin the property in question.

(t) That your taxpayer has in good faith endeavored to form a practical scheme to transform the use of said property or some part thereof to some other business and has considered transforming the same into a dairy plant, into an ice-cream factory, into a cold-storage plant, and into an ice-manufacturing plant, which were the only kinds of business to which said buildings are at all adaptable, to the best of your petitioner's knowledge, information, and belief. The officers and agents of your petitioner consulted with many persons learned and skilled in the several businesses, arts, and sciences
14 above set forth, who inspected the premises and, as your petitioners are informed and verily believe, the said buildings as

well as the said machinery, works, equipment, furniture, fixtures, and plant of your petitioners are not adapted to any such businesses or adaptable thereto by the expenditure of any reasonable amount of disbursements therefor. Your petitioners do not know of any business to which said buildings, plant, works, machinery, equipment, furnishings, and fixtures are adaptable except the business of producing and selling malt and spirituous liquors, which, by the incidence, promulgation, and enforcement of said constitutional amendment and said statutes, has become unlawful.

(u) That the assessed valuation of said real property of the taxpayer by the assessor of the city of Niagara Falls was reduced 42 per cent because of the effect upon said property by the incidence and promulgation of said statutes and constitutional amendment; that said real property is now valued by said assessor at $104,760, including the buildings and improvements thereof, whereas the same was valued prior to the incidence and promulgation of said statutes and constitutional amendment at $183,460, and that the rate of equalization of said taxes in the year 1918, by the New York State Board of Equalization, was 91 per cent and the rate of equalization thereof in 1924 was per cent.

(v) On October 28, 1919, the taxpayer petitioner abandoned the entire lower story, consisting of storage space, of a stone building consisting of three stories and a loft. The third story and loft were abandoned prior to 1918. The space abandoned in October, 1919, consisted of four cellars or storage spaces used for the storage of beer prior to the incidence and promulgation of the said acts of Congress and constitutional amendment. This space was useless in the manufacture of malt and cereal beverages containing less than one-half of one per cent of alcohol, and the entrance stairway to this storage space was closed up by the taxpayer on or about the date mentioned. The value of this one-third of said building on October 28th, 1919, was in excess of $23,626.83. This building is shown as building number four on the plan of the American Appraisal Company, dated November, 1912.

(w) Building number three, as shown upon said plan, consisted of two parts. The easterly part of this building was rebuilt in 1917 by taxpayer to house new improved storing material, filtering machinery, and bottling machinery, which was purchased for installation. The cost of reconstruction of the building and the purchase and installation of the machinery was $45,142.56. Said building was of the value of $79,633.11 on December 31st, 1918. Upon the incidence of the said statutes and the said constitutional amendment the easterly one-half of said building, newly constructed, together with the equipment therein, became almost entirely useless, and the use of the machinery and building was reduced by the incidence of said statutes and constitutional amendment to five per cent of the use thereof prior to the incidence of said statutes and constitutional amendment. Said building and machinery were used after October 28, 1919, approximately one day in every three weeks. The tax-

payer abandoned the use of the easterly one-half of said building and machinery except said five per cent use referred to.

(x) That all of said machinery, buildings, works, furnishings, fixtures, and equipment are owned by the taxpayer petitioner free from incumbrances in fee simple absolute.

(y) The taxpayer petitioner in the course of its business built up and acquired a good will and valuable trade-names by means of the quality of its service, its advertising, and the quality of its
16 product. The good will and these trade-names were intangible assets of the taxpayer and of greater value than the amount of said obsolescence deductions computed and claimed by the taxpayer on its income-tax returns. By the incidence of said statutes and constitutional amendment said good will and trade-names of the taxpayer were destroyed and reduced in value and rendered obsolete. Upon the computation of invested capital made by the Income Tax Bureau herein, resulting in the assessment upon which this appeal is filed, the taxpayer's good will, trade-names, and trade-marks are valued as follows:

Average income of taxpayer for pre-war period		$ 842,406.24
Average capital and surplus, same period	$8446,068.01	
Average loans and mortgages, same period	53,593.86 @ 5%	2,679.69
Leaving average working capital and surplus, same period	392,474.15	
And average working income, same period		39,726.55
Average working capital should earn 8%, or		31,397.93
Average income not attributable to working capital and attributable to intangibles		8,328.62
Which, capitalized @ 15%, is the assured value of the intangibles		55,524.13

17 (z) All of said assets, including said buildings, machinery, equipment, fixtures, good will, trade-names, trade-marks, and other assets, were used by the taxpayer in its trade or business above described.

6. The taxpayer in support of its appeal relies upon the following propositions of law:

(a) The depreciation in the value of the assets hereinbefore described, due to the incidence and promulgation of said statutes and constitutional amendment, constituted obsolescence.

(b) The depreciation in the value of the assets hereinbefore described, due to the incidence and promulgation of said statutes and constitutional amendment, constituted losses sustained by the taxpayer not compensated for by insurance or otherwise and incurred in the trade or business of the taxpayer.

(c) The amount written off by the officers, agents, and directors of the taxpayer, to wit, $110,047.52 in the year 1918 and $57,139.99 in the year 1919, was a reasonable allowance for such obsolescence or less than such a reasonable allowance and the amount or less than the amount of the losses sustained.

(d) The taxpayer abandoned property consisting of the lower story of building number four and the easterly one-half of build-

ing number three to more than the amount of the loss and absolescence deducted.

(e) By and in undertaking the business of producing soft drinks and cereal beverages containing less than one-half of one per cent of alcohol by volume, and in ceasing to continue its business of brewing spirituous and malt liquors, the taxpayer abandoned the said property and all of its property devoted to the business of brewing spirituous and malt liquors as a matter of law.

(f) The taxpayer, under and by virtue of section 214 of the income tax law for 1918, is entitled to deduct the
18 amount of such obsolescence without any abandonment of the property which has become obsolete.

Wherefore the taxpayer and the other petitioners respectfully pray that this board may hear and determine their appeal, may cancel and annul said additional assessment, and may render to the taxpayer such other and further relief as may be just in the premises.

Niagara Falls Brewing Company, by George F. Nye, president; Paul A. Schoellkopf, Chas. E. Haeberle, Fred H. Krull, Edson P. Pfohl, Albert T. Mayle, Frederick Chormann, Rudolf V. Rose, George F. Nye, directors of taxpayer, as trustees in dissolution.

BASIL ROBILLARD,
Attorney in Fact, and Counsel for said Taxpayer and Petitioners.

Office and P. O. address, 425–443 Gluck Building, Niagara Falls, N. Y.

19 [*Duly sworn to by George F. Nye and Rudolf V. Rose; jurat omitted in printing.*]

20 *Schedule A to petition*

Address reply to Commissioner of Internal Revenue and refer to IT:CA:2225–12.

OFFICE OF COMMISSIONER OF INTERNAL REVENUE,
TREASURY DEPARTMENT,
Washington, Nov. 26, 1924.

NIAGARA FALLS BREWING COMPANY,
Niagara Falls, New York.

SIRS: In accordance with the provisions of section 274 (d) of the revenue act of 1924, there has been assessed against you an income and excess-profits tax amounting to $25,988.70 for the taxable years 1918 and 1919, the details of which are set forth in the attached statements.

Under the provisions of section 279 (a) of the act you have the right to file with the collector of internal revenue, within ten days after notice and demand for payment, a claim for abatement of this tax or any part thereof. The claim should have attached to it all evidence and data upon which you rely in support thereof, and should be accompanied by a bond not exceeding double the amount of the claim, with such sureties as the collector deems necessary. When the claim is received by the collector, it will be transmitted to the Commissioner of Internal Revenue, Washington, D. C., who will notify you of the action taken.

Respectfully,

J. G. BRIGHT,
Deputy Commissioner.

Enclosures: Statements.

21 IT:CA-2225-12.

STATEMENT.—*In re Niagara Falls Brewing Company, Niagara Falls, New York*

	Deficiency in tax	Overassessment
1918	$20,975.05	
1919	5,013.65	
1920		$1,325.94
1921	None.	
1922	None.	
Totals	25,988.70	1,325.94
Net deficiency in tax	$24,662.76	

You are advised that the adjustments made by the revenue agent in his report as to the net income and adjusted invested capital have been accepted by this office.

The overassessment recommended by the revenue agent for the year 1918 in the amount of $29,799.00 has been corrected due to the fact that the revenue agent assumed that $50,744.05 had been assessed, which was erroneous. Therefore, inasmuch as the true tax liability is $20,975.05 and no tax has been assessed, there is a tax due of the amount mentioned.

For the year 1919 a similar change is made from an overassessment recommended by the revenue agent in the amount of $2,485.53 to an additional tax of $5,013.35 for the reason that the revenue agent erroneously assumed the additional tax outlined in office letter dated January 8, 1924, had been assessed.

By virtue of the adjustments made by the revenue agent in the report which has been accepted by this office as correct, office letter dated January 8, 1924, proposing an additional tax liability based upon adjustments made in this office is hereby annulled.

22 *Schedule B to petition*

NOTICE AND DEMAND FOR INCOME TAX

Form 7658—Revised July, 1924

United States Internal Revenue Service

Notice is hereby given that there has been assessed against you the amount stated hereon. Demand is hereby made for immediate payment of said tax. If payment is not made within ten days after date of this notice, the act provides that interest at the rate of 1 per cent per month will accrue from the due date.

Dated ———. Date, ———. Collector's (Paid) stamp.

To the COLLECTOR OF INTERNAL REVENUE AT BUFFALO, N. Y.:

I inclose herewith the sum of $—— in payment of the tax shown below.

Name, ——— ———. Address, ———.

Name and address	Items	Total assessment
Niagara Falls Brewing Co., Niagara Falls, N. Y.	1918 1120 RAR SEC 274D OL 11-26-24	$30,975.05 Credit 1,425.94 overassessment for 1920
Dec 00 C PL No. 2.	Waiver	14,049.11

Collector: Withhold demand pending comparison with Schedule of Overassessment (Form 7805) No. 12502.

Return this form with remittance.

23 NOTICE AND DEMAND FOR INCOME TAX

Form 7658—Revised July, 1924

United States Internal Revenue Service

Notice is hereby given that there has been assessed against you the amount stated hereon. Demand is hereby made for immediate payment of said tax. If payment is not made within ten days after date of this notice, the act provides that interest at the rate of 1 per cent per month will accrue from the due date.

Dated ———. Date, ———. Collector's (Paid) stamp.

To the COLLECTOR OF INTERNAL REVENUE at Buffalo, N. Y.

I inclose herewith the sum of $—— in payment of the tax shown below.

Name, ——— ———. Address, ———.

Name and address	Items	Total assessment
Niagara Falls Brewing Co., Niagara Falls, N. Y.	1919 1120 RAR SEC 274D OL 11-26-24	$3,013.63
DEC 01 C SPL No. 2		

Collector: Withhold demand pending comparison with schedule of overassessment (Form 7805) No. 12502.

Return this form with remittance.

24 *Schedule C to petition*

Treasury Department

Internal Revenue Service

OFFICE OF THE COLLECTOR,
TWENTY-EIGHTH DISTRICT OF NEW YORK,
Buffalo, N. Y., January 5, 1925.

3199-CJP.

NIAGARA FALLS BREWING CO.,
George F. Nye, Liquidating Agent,
Niagara Falls, N. Y.

GENTLEMEN: Enclosed are demand notices, Form 7658, for additional income and profits taxes assessed by the commissioner for years 1918 and 1919, less over-assessment for the year 1929, in the net aggregate amount of $24,662.76.

These taxes are entitled to be paid before all other claims, the priority of the United States for the payment of taxes being fully determined by section 3466 of the Revised Statutes.

And attention is hereby called to section 3467 of the Revised Statutes, which provides that every executor, administrator, or assignee, or other person who pays any debt due by the person or estate from whom or for which he acts, before he satisfies and pays the debts due to the United States from such person or estate, shall become answerable in his own person and estate for the debts so due to the United States, or for so much thereof as may remain due and unpaid.

Respectfully,

BERT P. GAGE, *Collector,*
By CHAS. J. PETERS,
Head of Division.

Enc.: R

25 *Schedule D to petition*

(Execute separate form for each tax period)

Treasury Department, Internal Revenue Service.
Form 843—Jan. 1922 Comptroller General U. S. January 18, 1922

IMPORTANT.—File with collector of internal revenue where assessment was made. Not acceptable unless completely filled in.

CLAIM FOR

X Abatement of tax assessed
Credit against outstanding assessments
Refund of taxes illegally collected
Refund of amounts paid for stamps used in error or excess

NOTICE TO COLLECTOR.—Collector must indicate in block above the kind of claim, except in income tax cases.

Date received by administrative unit—Schedule D—(stamp here) ———.

Collector's notation: District, ———. Account number, ———. Date received, ——— (stamp here). ——— ———, collector of internal revenue.

STATE OF NEW YORK,
County of Niagara, ss:

NIAGARA FALLS BREWING COMPANY,
(Name of taxpayer or purchaser of stamps)

None.
(Residence—give street and number as well as city or town and state)

732 Third Street, Niagara Falls, New York.
(Business address)

This deponent, being duly sworn according to law, deposes and says that this statement is made on behalf of the taxpayer named, and that the facts given below with reference to said statement are true and complete:

		Period	Year
		From Jan. 1	1919
		To Dec. 31	1919
1	Business in which engaged. Brewing of malt beverages		
2	Character of assessment or tax. Income and excess profits tax (state fully upon what the tax was assessed or the stamps affixed)		
3	Amount of assessment or stamps purchased		$25,000.00
4	Reduction of tax liability requested (income and profits tax)		25,000.00
5	Amount to be abated		25,000.00
6	Amount to be refunded (or such greater amount as is legally refundable)		None
7	Dates of payment (see collector's receipts or indorsements of canceled checks) (If statement covers income tax liability items 8 to 11 inclusive must be answered.)		
8	District in which return of same was filed. 28th New York		
9	District in which unpaid assessment appears. 28th New York		
10	Amount of overpayment claimed as credit		
11	Unpaid assessment against which credit is asked		
	Period from Jan. 1 1918 to Dec. 31 1918		$20,075.66
	Jan. 1st 1919 to Dec. 31st 1919		5,924.34

Deponent verily believes that this application should be allowed for the following reasons:

Said assessment was made pursuant to section 274 (d) of the revenue act of 1918, as set forth in a letter dated November 26, 1924, from J. O. Wright, deputy commissioner, under the symbols IT:CA 2222-12, copy of which letter is hereto annexed and made a part of this claim for abatement. Credit has been allowed against the assessment for 1918 in the sum of $4,925.94 on account of overassessment for the year 1920.

Deponent respectfully refers to the notice of appeal under symbols IT:CA:N–S–JJL–2122–11–APP, filed in this matter with the Commissioner of Internal Revenue on or about January 24th, 1924, and to the affidavit of Samuel W. Glasz, verified February 29th, 1924, together with the schedules, photographs, and photostats thereto annexed, filed with the said Commissioner of Internal Revenue
26 on or about February 29th, 1924; the affidavits of W. D. Uptegraff, John J. Foley, Frank E. Giroux, A. E. Eggleston, Charles J. Deckop, and Sutton, filed with the Commissioner of Internal Revenue on or about November 22, 1923; the letter of the taxpayer, dated June 11, 1923, filed with the Commissioner of Internal Revenue under said symbols on or about June 11, 1923; proof of the authority of deponent to act for said corporation, verified by the secretary of said corporation and of its board of directors acting as trustees in dissolution, on or about June 15, 1924; and all other papers and documents filed by the taxpayer and its trustees in dissolution with said Commissioner of Internal Revenue in and in connection with the matter of proposed additional assessment of income tax against said taxpayer for the years 1918 and 1919 under symbols IT:CA:M–2–JJL–2122–11–APP, and makes the same a part of this claim for abatement by reference as though they were hereto physically annexed.

GEORGE F. NYE,
Liquidator Appointed by Trustees in Dissolution and One of said Trustees.

Sworn to and subscribed before me this 15th day of January, 1925.
[NOTARIAL SEAL.]
PAUL P. COHEN,
Notary Public, Erie County.
Certificate filed, Niagara County.

27 *Schedule E to petition*

KNOW ALL MEN BY THESE PRESENTS:

That we, Niagara Falls Brewing Company, a corporation organized under the laws of the State of New York, having its principal place of business at 732 Third Street, in the city of Niagara Falls, New York, as principal and United States Fidelity & Guaranty Company, of Baltimore, Md., as surety, are held and firmly bound unto the United States of America and Bert P. Gage, collector of internal revenue for the 28th district of New York, hereinafter referred to as the "collector" in the just and full sum of thirty five thousand dollars ($35,000) lawful money of the United States, for which payment, well and truly to be made, we bind ourselves, our successors and assigns, jointly and severally, firmly by these presents.

Sealed with our seals, and dated the 15th day of January, 1925.

Whereas a deficiency in income and excess profits taxes for the taxable years 1918 and 1919, amounting to $25,988.70, has been as-

sessed against the above-named Niagara Falls Brewing Company by the Commissioner of Internal Revenue, hereinafter referred to as the "commissioner," which assessment appears upon the collector's December, 1924, special No. 2 income-tax assessment list at page 0, lines 0C and 1C; and

Whereas the said Niagara Falls Brewing Company in conformity with the provisions of sections 279 and 280 of the revenue act of 1924, has filed with the collector a claim for the abatement of the whole of such deficiency.

28 Now, therefore, the condition of this obligation is such that if the said Niagara Falls Brewing Company shall, upon notice and demand by the collector, well and truly pay or cause to be paid to the collector, at his office in the Federal Building, in the city of Buffalo, New York, so much of the amount of said claim as shall at the time of said notice and demand have been denied by the commissioner, or by the Board of Tax Appeals, if an appeal to said board shall have been lawfully taken, together with all interest and penalties thereon that may be lawfully asserted at the date of such payment, then the above obigation shall be void and of no effect; otherwise to be and remain in full force and virtue.

In witness whereof the said Niagara Falls Brewing Company and the said United States Fidelity & Guaranty Company have hereunto caused their corporate seals to be affixed and these presents to be affixed by their proper officers thereunto duly authorized.

NIAGARA FALLS BREWING COMPANY,
By GEORGE F. NYE, *Liquidator.*

Attest:
EDSON P. PFOHL.
[Seal of Niagara Falls Brewing Co.]

UNITED STATES FIDELITY & GUARANTY COMPANY,
By WILLIAM H. KENNEDY, *Attorney in Fact.*

Attest:
HELEN G. KENNEDY,
Attorney in Fact.
[Seal of United States Fidelity & Guaranty Co.]

29 STATE OF NEW YORK,
County of Niagara, ss:

On this 15th day of January, 1925, before me personally came George F. Nye, to me known, who, being by me duly sworn, did depose and say that he resides in the city of Niagara Falls, New York; that he is the liquidator of Niagara Falls Brewing Company, one of the corporations described in and which executed the foregoing instrument; that he knows the seal of said corporation; that the seal affixed to said instrument is such corporate seal; that it was so affixed by order of the board of directors of said corporation and that he signed his name thereto by like order.

[NOTARIAL SEAL.] PAUL P. COHEN,
Notary Public, Erie County,
Certificate filed, Niagara County.

30 *Schedule F to petition*

TREASURY DEPARTMENT,
OFFICE OF COMMISSIONER OF INTERNAL REVENUE,
Washington, Aug. 13, 1925.

IT:CA:2227–6.

NIAGARA FALLS BREWING COMPANY,
732 Third Street, Niagara Falls, New York.

SIRS: A reaudit of your income-tax returns for the years 1918 and 1919 in connection with your claim for abatement of tax assessed in the amount of $25,988.70 discloses no additional tax nor overassessment. Your claim will, therefore, be rejected in full.

In accordance with the provisions of section 279 (b) of the revenue act of 1924 you are allowed 60 days from the date of this letter within which to file an appeal to the Board of Tax Appeals contesting in whole or in part the correctness of this determination.

If you acquiesce in this determination and do not desire to file an appeal, you are requested to sign the enclosed agreement consenting to the assessment of the deficiency and forward it to the Commissioner of Internal Revenue, Washington, D. C., for the attention of IT:CA:2227–6. In the event that you acquiesce in a part of the determination, the agreement should be executed with respect to the items agreed to.

Respectfully,

D. H. BLAIR,
Commissioner.
By J. G. BRIGHT,
Deputy Commissioner.

Enclosures: Statements; agreement, Form B.

31 IT:CA:2227–6

STATEMENT.—*In re Niagara Falls Brewing Company, Niagara Falls, New York*

1918

ADJUSTMENTS TO INCOME

Net loss reported		$1,295.91
Additions to income:		
1. Donations	$1,520.00	
2. Excessive depreciation	288.00	
3. Obsolescence	110,047.52	
Total additions		111,855.52
Total		110,559.61
Deductions from income:		
4. Excise tax, 1912	$96.69	
5. Additional depreciation	3,434.75	
6. Loss on casks and tanks scrapped	18,210.16	
Total deductions		21,741.60
Net income as adjusted		88,818.01

Explanation of adjustments

1. Donations are disallowed in accordance with article 562, Regulations 45.

2. Depreciation for 1917 on outside properties sold in 1918 disallowed as a loss in 1918. The depreciation was allowed as a deduction from 1917 income.

32 3. Obsolescence claimed on account of legislation adverse to the brewing trade, amounting to $110,047.52. After careful consideration of all information submitted this office holds that, for the reason that the taxpayer continued in a similar or related business subsequent to the enactment of national prohibition, no allowance may be made for the obsolescence of the good-will valuation attaching to the business as of March 1, 1913. For the further reason that the cost on March 1, 1913, value of the assets claimed to have been abandoned has not been established or complete abandonment in respect to any assets, as a unit, has not been shown, it is held that no obsolescence may be allowed on tangibles.

4. Excise tax for 1912 in the amount of $96.69 paid in 1918 was held at date of revenue agent's report to be an allowable deduction from gross income. Under I. T. (supra) 2011 this tax is not an allowable deduction; however, since any additional tax caused by the disallowance of this item is outlawed, the deduction is allowed to stand.

5. Depreciation as shown in the revenue agent's report, dated October 17, 1924, a copy of which was furnished you, has been accepted by this office. There is a further deduction for depreciation of this amount allowable.

6. Loss on casks and tanks scrapped:

March 1, 1913, value		$27,643.00
Depreciation to January 1, 1913	$6,668.54	
Depreciation, 1913 to 1917, inclusive, 5 years at 2%	2,754.30	
		9,432.84
Loss allowed		18,210.16

33 INVESTED CAPITAL

Invested capital at beginning of year as disclosed by books		$516,472.57
Addition:		
1. Real estate	$25,000.00	
2. Buildings	8,328.81	
3. Machinery and equipment	25,745.78	
4. Depreciation disallowed prior years	22,798.81	81,873.40
Total		589,345.97
Deduction:		
5. 1917 Federal tax prorated	$1,218.53	
6. Additional tax prior to above	870.50	
		2,089.03
Invested capital as adjusted		596,256.94

Explanation of adjustments

1. This represents depreciation charged off and credited to asset in 1915. The depreciation was not deducted on the return for 1915 and has never been allowed.

2. Depreciation charged off on outside properties and credited to the asset in prior years restored and credited to reserve for depreciation.

3. Depreciation charged off on small cooperage and credited to asset in prior years restored and credited to—

Reserve for depreciation	$15,745.78
Improvements in 1917 disallowed as expense	10,000.00
	25,745.78

34 4. Decreases and increases shown in Exhibit A of the revenue agent's report, dated October 17, 1924, a copy of which has been furnished you.

5 and 6. Income and profits taxes are deemed to be paid from earnings of the year for which they are assessed and are allowable in computing invested capital to the dates payable. 1917 taxes were payable June 15, 1918; hence $2,223.81 prorated for 200 days is deducted. Additional taxes for years prior to 1917 were all payable prior to January 1, 1918; therefore are deducted in full.

COMPUTATION OF TAXES

Net income			$88,818.01
Invested capital			596,256.94
Excess-profits credit			50,700.56
War-profits credit			73,822.43
Total profits tax			11,996.46
Net income		$88,818.01	
Less:			
Profits tax	$11,996.46		
Exemption	2,000.00		
		13,996.46	
Balance subject to tax at 12%		74,821.55	8,978.59
Total tax assessable			20,975.05
Tax previously assessed			20,975.05
Deficiency or overassessment			None.

35 1919

ADJUSTMENTS TO INCOME

Net income reported		$3,526.23
1. Donations	$420.88	
2. Obsolescence	57,139.99	
		57,569.87
Total		61,096.10
Deductions:		
3. Liberty-bond interest	220.10	
4. Additional depreciation	7,350.34	
		7,570.44
Net income as adjusted		53,525.66

Explanation of adjustments

1. Donations are disallowed in accordance with Article 562, Regulations 45.

2. Obsolescence claimed on account of legislation adverse to brewing trade. The reasons for this disallowance is fully explained under 1918 explanation of adjustment to income #3.

3. Liberty-bond interest amounting to $220.10, which is exempt from income tax.

4. Depreciation as shown in the revenue agent's report, dated October 17, 1924, a copy of which was furnished you, has been accepted by this office.

36 COMPUTATION OF TAX

Excess-profits credit exceeds net income; therefore there is no excess profits tax.

Net income	$53,525.93	
Less exemption	2,000.00	
Balance subject to tax	51,525.93	
Amount of tax at 10%		5,152.57
Total tax assessable		5,152.57
Total tax previously assessed		5,152.57
Deficiency or overassessment		None.

37 *Schedule G to petition*

At a special term of the supreme court held in and for the Eighth Judicial District at the city and county hall, in the city of Buffalo, Erie County, New York, on the 22 day of December, 1921.

Present: Hon. Wesley C. Dudley, justice, presiding.

Supreme Court, Niagara County

In the matter of the dissolution of Niagara Falls Brewing Company, a New York State corporation having its office and principal place of business in the city of Niagara Falls, Niagara County, N. Y., pursuant to the provisions of sec. 221 of the general corporation law of the State of New York

On reading and filing the petition of Niagara Falls Brewing Company, bearing date the 21st day of December, 1921, and duly verified by George F. Nye, its president, wherein and whereby it appears that said corporation has been duly dissolved pursuant to the provisions of section 221 of the general corporation law of the State of New York, and praying for an order of this court—

38 (a) Naming a newspaper or newspapers for the purpose of publishing notice to creditors.

(b) Designating the form in which such notice to creditors shall be published,

(c) Specifying the length of time and manner in which such notice shall be published, and

(d) For such other, further or different relief as may be just and proper,

and after hearing Frederick Chormann, Esq., of counsel in favor of this motion

Now, on motion of Cohn, Chormann & Franchot, attorneys for the petitioner, it is

ORDERED: 1. That notice to creditors in the form herein provided be published once a week for three weeks in the Niagara Falls Gazette, a newspaper published in the city of Niagara Falls, New York, and having a general circulation within said city and within the county of Niagara, which is the county wherein the principal place of business of said Niagara Falls Brewing Company was located.

2. That the form of notice to creditors so to be published be substantially as follows:

NOTICE TO CREDITORS

Notice is hereby given that the Niagara Falls Brewing Company, a corporation organized and existing under and by virtue of the laws of the State of New York, having its principal place of business in the city of Niagara Falls, N. Y., has been dissolved pursuant to the provisions of section 221 of the general corporation law of the State of New York, and that all persons having claims against
39 the above-named corporation are hereby directed to present the same, duly verified, at the office of the corporation on Third Street in the city of Niagara Falls, N. Y., on or before the 16th day of January, 1922.

NIAGARA FALLS BREWING COMPANY,
By (here insert names of the nine directors),
Directors Acting as Trustees in Dissolution.

and that the publication of such notice, substantially in the form herein provided and in the manner herein provided, shall be deemed ample and sufficient.

WESLEY C. DUDLEY, *J. S. C.*

Erie special term, Dec. 22, 1921. Granted and ordered entered in Niagara county clerk's office.

G. V. LAUGHLIN, *Sp. Dep. Clerk.*

Now, August 5, 1929, the foregoing petition certified from the record as a true copy.

[SEAL.]

B. D. GAMBLE,
Clerk, U. S. Board of Tax Appeals.

40 Before United States Board of Tax Appeals

[Title omitted.]

Answer

Filed Nov. 3, 1925

The Commissioner of Internal Revenue, by A. W. Gregg, Solicitor of Internal Revenue, his attorney, for answer to the petition heretofore filed by the above-named taxpayer, admits and denies as follows:

1. Admits the allegations of paragraphs numbered 1, 2, and 3.

2. Admits the allegations of sub-paragraph (a) of paragraph 5, except that he denies that the use of the buildings, machinery, fixtures, and equipment for the purpose of making and selling soft drinks was to a minor extent only as alleged by the taxpayer.

3. Admits that the buildings, machinery, fixtures, and equipment were acquired for the most part prior to March 1, 1913.

4. Denies that the fair market value of said buildings, machinery, fixtures, and equipment as of March 1, 1913, was as alleged by the taxpayer (b) of paragraph 5.

41 5. Denies that the soft-drink department, machinery, and equipment were acquired by the taxpayer after March 1, 1913, at a cost of $4,533.09.

6. Neither admits nor denies the taxpayer's allegations concerning the adoption of the eighteenth amendment to the Constitution of the United States and concerning the various acts of Congress and proclamation of the President set forth by the taxpayer in sub-paragraphs (c), (d), (e), (f), (g), and (h), and asks the board to take judicial notice of the state of the law relating to intoxicating beverages.

7. Admits the allegations of sub-paragraph (i) of paragraph 5.

8. Denies the allegations of sub-paragraph (j) of paragraph 5.

9. Admits that during the calendar year 1918 the officers of the taxpayer caused to be charged off the books of the taxpayer the amount stated in sub-paragraph (k) of paragraph 5.

10. Admits that the officers of the corporation caused to be charged off the taxpayer's books during the year 1919 the amount stated in sub-paragraph (l) of paragraph 5.

11. Denies the allegations of sub-paragraph (m) of paragraph 5.

12. Admits the allegations of sub-paragraph (n) of paragraph 5, except that he denies that the property was prior to the going into effect of prohibition entirely devoted to the manufacure of spirituous and malt liquors.

13. Admits the allegations of sub-paragraphs (c) and (p) of paragraph 5.

14. Admits the allegations of sub-paragraph (q) of paragraph 5, except that he denies the taxpayer's conclusions concerning the value indicated by the capitalization of rent.

42 15. Admits the allegations of sub-paragraph (r) of paragraph 5.

16. Denies the allegations of sub-paragraph (s) of paragraph 5.
17. Denies the allegations of sub-paragraph (t) of paragraph 5.
18. Denies the allegations of sub-paragraph (u) of paragraph 5.
19. Denies the allegations of sub-paragraphs (v), (w), (x), and (y) of paragraph 5.
20. Admits the allegations of sub-paragraphs (z) of paragraph 5.
21. Denies generally and specifically each and every allegation not hereinbefore admitted, qualified or denied.

PROPOSITION OF LAW

The taxpayer is not entitled to a deduction for obsolescence of tangible and intangible property due to the incidence of prohibition legislation.

Wherefore it is prayed that said petition be denied.

A. W. GREGG,
Solicitor of Internal Revenue,
Attorney for Commissioner of Internal Revenue.

Of counsel:
JOHN D. FOLEY,
Special Attorney, Bureau of Internal Revenue.

Now, August 5, 1929, the foregoing answer certified from the record as a true copy.

[SEAL.] B. D. GAMBLE,
Clerk, U. S. Board of Tax Appeals.

43 Before United States Board of Tax Appeals

[Title omitted.]

Amendment to petition

Filed Dec. 16, 1925

To the United States Board of Tax Appeals:

The Niagara Falls Brewing Company, a corporation of the State of New York, and Paul A. Schoellkopf, Charles E. Haeberle, Fred H. Krull, Edson P. Pfohl, Albert T. Mayle, Frederick Chormann, Rudolf V. Rose, and George F. Nye, as directors of said company and trustees thereof in dissolution, hereby move your honorable board for an order granting to them leave to amend their petition for appeal herein, verified October 7th, 1925, and filed with your honorable board October 10th 1925, by adding thereto at the end of paragraph 4 on page 3 thereof as subdivision (c) of said paragraph the following:

"(c) Said assessments are contrary to the revenue act of 1918 and the acts amendatory thereof and supplemental thereto and the regulations of the Treasury Department promulgated in pursuance thereof, in that in computing invested capital for the purpose of

assessing said tax the commissioner erroneously reduced the
44 proper invested capital of said company by a prorated part of the income and excess profits taxes paid by said company for the years 1917, 1918, and 1919, contrary also to the decision of the United States Board of Tax Appeals in the Appeal of Guaranty Construction Company, Docket Nos. 1828 and 1848, decided October 30th, 1925."

Said allegation was not contained in the said petition for appeal because the said decision of this board had not been made or promulgated at that time.

No previous application for leave to amend said petition for appeal has been made herein.

Wherefore petitioners pray for an order of this board granting leave to said petitioners to amend said petition for appeal by the insertion of said paragraph.

Dated, December 10th, 1925.

Respectfully submitted.

Basil Robillard, attorney & counsel for Niagara Falls Brewing Co.; Paul A. Schoellkopf, Charles E. Haeberle, Fred H. Krull, Edson P. Pfohl, Albert T.
[SEAL.] Mayle, Frederick Chottmann, Rudolf V. Rose, and George F. Nye, petitioners, office & P. O. address 426-443 Gluck Building, Niagara Falls, New York.

Now, August 5, 1929, the foregoing amendment to petition certified from the record as a true copy.

B. D. GAMBLE,
Clerk, U. S. Board of Tax Appeals.

45 Before United States Board of Tax Appeals

[Title omitted.]

Answer to amendment

Filed January 21, 1926

The Commissioner of Internal Revenue, by A. W. Gregg, Solicitor of Internal Revenue, his attorney, for answer to the amendment of the petition filed by the taxpayer December 14, 1925, admits that invested capital for the year 1918 has been reduced by the prorated amount of 1917 income and profits taxes, such proration being made on the basis of permitting the amounts of the 1917 income and profits taxes to remain in invested capital for the year 1918 until June 15, 1918; admits that he is in error in so doing and says that the amount of 1917 income and profits taxes should reduce invested capital as of December 31, 1917. He further says that for the year 1919 no profits tax is proposed for assessment.

PROPOSITION OF LAW

Amounts payable on account of Federal income and profits taxes for the preceding year may not, in accordance with section 326 of the revenue act of 1918, be included in invested capital for the taxable year.

A. W. GREGG,
Solicitor of Internal Revenue,
Attorney for Commissioner of Internal Revenue.

Of counsel:
JOHN D. FOLEY,
Special Attorney, Bureau of Internal Revenue.

NOW, August 5, 1929, the foregoing answer to amendment to petition certified from the record as a true copy.

[SEAL] B. D. GAMBLE,
Clerk, U. S. Board of Tax Appeals.

46 Before United States Board of Tax Appeals

NIAGARA FALLS BREWING COMPANY AND PAUL SCHOELLKOPF, CHARLES E. HACKETT, FRED H. KRULL, EDSON P. PFOHL, ALBERT E. MAYLE, FREDERICK CHORTMAN, RUDOLF V. ROSE, AND GEORGE F. NYE, as Directors and Trustees in Dissolution, petitioners

v

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

Docket No. 7962. Promulgated October 16, 1928

Findings of fact and opinion

1. Held, that the petitioner is not entitled to a deduction for obsolescence for intangible assets, including good will.

2. Where prior to enactment of wartime and permanent prohibition the petitioner had been engaged in the manufacture and sale of beer and "near beer" and after October 28, 1919, ceased to manufacture and sell beer but continued to make and sell "near beer," using the same machinery and process as had been previously used in the manufacture of beer with the exception of dealcoholization before bottling, held, that the petitioner is not entitled to a deduction for obsolescence on such property.

3. Evidence insufficient upon which to determine the amount of obsolescence sustained by the petitioner as a result of having abandoned the lower floor of one of its buildings as a result of having ceased to make beer.

4. Losses claimed as a result of the decrease in value of tangible assets continued in use denied.

47. Basil Robillard, Esq., and Edward C. Cornell, C. P. A., for the petitioner. M. E. McDermott, Esq., for the respondent.

(A true copy. Teste: B. D. Gamble, clerk U. S. Board of Tax Appeals. (Seal.))

This is a proceeding for the redetermination of deficiencies in income and profits taxes of $[illegible] for 1918 and income tax of $5,013.66 for 1919. The deficiencies result principally from the respondent's having disallowed for 1918 a deduction of $[illegible] and for 1919 a deduction of $[illegible]. The deductions were taken by the petitioner in its returns for the respective years as depreciation on tangible assets resulting from the enactment of war time prohibition legislation and the ratification of the eighteenth amendment. It was admitted by the respondent at the hearing that he had failed to allow as a deduction an amount of $[illegible] representing a part of a loss sustained on the sale of certain property in 1918. From the pleadings, a stipulation, documentary evidence and depositions we make the following

FINDINGS OF FACT

The petitioner, a New York corporation, was organized February [illegible], 1903, and had its office and place of business at Niagara Falls.

The business of the petitioner prior to the incidence of the eighteenth amendment to the Constitution of the United States and the acts of Congress in the enforcement thereof was the manufacture, production, distribution, and sale of a malt and spirituous liquor known as beer, containing more than one half of one per cent of alcohol by volume. The petitioner's business and good will were created by the manufacture and sale of such beverage. In 1903 the petitioner purchased the buildings and equipment of the Niagara Falls Brewing Company, a joint stock association existing in Niagara Falls, New York, and assumed the current liabilities of the association.

The petitioner thereafter constructed some new buildings and purchased and installed some additional machinery, fixtures, and equipment, all of which were specially constructed, designed, or adapted to the petitioner's business of manufacturing beer, and were not available or practicable or readily adaptable to other uses. This property and equipment were devoted solely to the business of the petitioner in making beer and "Pep" beer containing less than one half of one per cent of alcohol by volume prior to the incidence of war time prohibition and the eighteenth amendment and the statutes in enforcement thereof.

About July 1, 1918, the petitioner commenced the manufacture of soft drinks in a separate building with machinery distinct from that used in the manufacture of beer or cereal beverages and which was carried in a separate account on petitioner's books.

The making and sale of beer and malt and spirituous liquors was discontinued because of the incidence of the eighteenth amendment and the statutes in enforcement thereof, but the making and sale of soft drinks and of beer of an alcoholic content of less than one half

of one per cent continued after the incident of such amendment and statutes. Petitioner continued to make "near beer" after it had discontinued the manufacture of beer in order to see if the plant could be made to pay by making this product and also to keep the plant in action and save the machinery.

49 No part of the obsolescence or extraordinary depreciation taken by the petitioner for the year in question was computed upon or taken on account of the depreciation of buildings, machinery, and equipment used for the manufacture of soft drinks other than dealcoholized beer.

The investment in equipment for the manufacture of soft drinks other than dealcoholized beer and the depreciation accrued thereon were as follows:

	Investment	Depreciation
1914	$ [illegible]	
1915	[illegible]	[illegible]
1916	[illegible]	[illegible]
1917	[illegible]	[illegible]
1918	[illegible]	[illegible]

The buildings, machinery, and equipment for the manufacture of beer and malt and spirituous liquors were acquired for the most part prior to March 1, 1913, and the cost, accrued depreciation, and depreciated cost thereof on March 1, 1913, were:

	Cost	Accrued depr.	Depreciated cost
Land	$ [illegible]	$	$ [illegible]
Buildings	[illegible]	[illegible]	[illegible]
Machinery	[illegible]	[illegible]	[illegible]
Tanks and tanks	[illegible]	[illegible]	[illegible]
Horses, wagons, etc.	[illegible]	[illegible]	[illegible]
Office furn. & fix.	[illegible]	[illegible]	[illegible]
Auto trucks	[illegible]	[illegible]	[illegible]
Signs	[illegible]	[illegible]	[illegible]
Retail conveyance	[illegible]		[illegible]
Bottle furn. & fix.	[illegible]	[illegible]	[illegible]
Outside property	[illegible]		[illegible]
Total	[illegible]	[illegible]	[illegible]

On March 1, 1913, the plant and buildings had a value equal to the amount at which they were set up on the books.

50 The cost, accrued depreciation, and depreciated cost of the buildings, machinery, and equipment on December 31, 1917, were as follows:

	Cost	Accrued depr.	Depreciated cost
Land	$ [illegible]	$	$ [illegible]
Buildings	[illegible]	[illegible]	[illegible]
Machinery	[illegible]	[illegible]	[illegible]
Tanks and tanks	[illegible]	[illegible]	[illegible]
Horses, wagons, etc.	[illegible]	[illegible]	[illegible]
Office furn. & fix.	[illegible]	[illegible]	[illegible]
Auto trucks	[illegible]	[illegible]	[illegible]
Retail conveyance	[illegible]	[illegible]	[illegible]
Bottle furn. & fix.	[illegible]	[illegible]	[illegible]
Outside property	[illegible]	[illegible]	[illegible]
Total	[illegible]	[illegible]	[illegible]

At the end of 1917 petitioner's buildings and machinery had a value fully equal to that at which they were carried on its books.

The book cost and the net depreciated book cost of the fixed assets of the petitioner at December 31, 1918, and December 31, 1919, were:

	Dec. 31, 1918		Dec. 31, 1919	
	Book cost	Net depd. cost	Book cost	Net depd. cost
Land	$100,000.00	$100,000.00	$100,000.00	$100,000.00
Buildings	229,999.32	108,057.31	229,999.32	63,008.03
Machinery:				
Beer	131,675.21	32,500.00	134,542.63	19,966.71
Soft-drink	4,533.09	4,533.09	7,400.18	6,946.87
Casks & tanks	40,399.35	5,000.00	40,399.35	2,000.00
Horses, wagons, etc	8,638.50	1,000.00	8,570.50	932.00
Office furn. & fix	3,101.74	600.00	3,173.87	400.00
Auto trucks:				
Beer	15,283.85	3,000.00	15,568.60	3,284.75
Soft-drinks	500.00	500.00	775.80	675.80
Small cooperage	2,632.71	500.00	2,232.71	100.00
Saloon furn. & fix	28,383.06	100.00	28,733.06	0
Outside property	38,128.55	38,128.55	38,147.27	32,500.00
Totals	603,275.38	293,918.95	609,543.29	229,814.16

The above items of cost, accrued depreciation, and depreciated cost were determined by the respondent and accepted by the pe-
51 titioner. In determining the depreciated cost there has been used a rate of depreciation fixed by the respondent.

During 1917 and 1918 the petitioner's officers and directors were aware through brewers' associations and other agencies of the enactment of State and National legislation affecting its business as well as of the proposal and progress toward ratification of the eighteenth amendment. At different times during these years recently enacted or pending legislation regarding the brewing of malted liquors and the future prospects of the business as well as the future of the petitioner were discussed or considered by the executive committee of the board of directors, the board of directors, and the stockholders.

The board of directors of the petitioner at a meeting held November 26, 1918, authorized the president and auditor of the company to investigate and make a report on the question of lawful depreciation to be taken on the plant, property, and equipment of the company in view of the pending prohibition legislation in an amount which, in the judgment of the president and auditor, was just, lawful, and proper.

The charges against earnings for the year 1918 for depreciation and obsolescence as recorded on the petitioner's books and deducted in its return for that year were as follows:

	Regular depreciation	Obsolescence		Regular depreciation	Obsolescence
Buildings	$4,597.63	$27,014.33	Autos and trucks	$2,611.26	$2,204.40
Machinery	5,389.93	59,430.22	Small cooperage	650.00	2,132.71
Casks and tanks	2,619.51	16,212.87	Saloon furn. and fix	833.21	522.01
Horses, wagons, etc	862.98	1,268.56			
Office furn. and fix	152.48	532.42	Total	17,117.30	110,047.52

52 The amount of the deduction for obsolescence was determined after discussions between the president, secretary, auditor, and brew master of the petitioner and after they had made surveys of the plant and machinery. The obsolescence taken was only on property that had been used to brew beer. The deduction for obsolescence represented the amount necessary to be written off the assets to bring them down to an amount which the petitioner's directors thought could be realized on them at a forced or liquidation sale after the imminent prohibition legislation should become effective. The amount of the deduction taken was determined after inquiries by the president of the petitioner as to what the brewing machinery would bring in the case of prohibition. The deductions for depreciation and obsolescence were approved by the board of directors on February 5, 1919, and by the stockholders of the petitioner on February 11, 1919.

During 1919 in addition to regular depreciation there were written off on petitioner's books additional amounts for obsolescence of property for which deductions for obsolescence had been taken for the prior year. The amounts written off in 1919 were based, among other things, on the fact that the assets of a similarly situated brewing company at Niagara Falls, which had taken greater deductions for obsolescence than the petitioner, had been sold in 1919 for only a fractional part of the amount at which the assets remained on the books. Other considerations were that the petitioner had to curtail the brewing of beer considerably more than theretofore, and that in the event that it attempted to dispose of its machinery it would not find any market because of so much of that kind of machinery being offered for sale.

The charges against earnings of the year 1919 for depreciation and obsolescence as recorded on the books of the petitioner and dededucted in its return for that year were:

53	Regular depreciation	Obsolescence		Regular depreciation	Obsolescence
Buildings	$5,049.28	$40,000.00	Small cooperage	$400.00	0
Machinery	5,854.02	10,000.00	Saloon furni. and fix	0	$450.00
Casks and tanks	2,071.52	928.48	Outside property	0	5,647.27
Office furni. and fix	157.89	114.24			
Auto trucks	100.00	0	Total	13,632.71	57,139.99

In a determination of the deficiencies herein involved the respondent disallowed the deductions taken by the petitioner for obsolescence and allowed deductions for depreciation and losses, as follows:

	Claimed on original return	Allowed by respondent	Difference
1918			
Regular dep'n	$17,117.30	$20,552.05	$3,434.75
Obsolescence	110,047.52	0	(110,047.52)
Loss, casks, & tanks		18,210.16	18,210.16
	127,164.82	38,762.21	(88,402.61)
1919			
Regular dep'n	13,632.71	20,983.05	7,350.34
Obsolescence	57,139.99	0	(57,139.99)
	70,772.70	20,983.05	(49,789.65)

The petitioner gave up and abandoned the manufacture and sale of beer in 1919 on account of the restrictions imposed by statute.

The petitioner's officers considered selling or converting its buildings and machinery into a plant for a dairy, cold storage, ice-cream manufacturing, dry storage, ice manufacture, fruit storage, semicold storage, machine shop, and chemical plant. The president of the petitioner, who was familiar with the use of buildings for industrial purposes, could find no use for the buildings and machinery except for the purpose of brewing beer or making cereal beverages. Because of the buildings being damp, the floor levels uneven, there being no elevators and but few openings for light, they were not readily adaptable for storage, manufacturing, or industrial purposes.

54 The buildings were zoned under the city zoning law in an industrial or manufacturing zone.

Much of the brewing machinery could not be removed from the buildings without tearing out the walls of the buildings or dismantling the machinery, and some of the machinery could not be dismantled to the extent that it could be removed without tearing out a side of the building.

Sales of the petitioner's products for the years 1912 to 1921, inclusive, were as follows:

	Barrels		Soft drinks		Barrels		Soft drinks
	Beer	Cereal beverage			Beer	Cereal beverage	
1912	33,177			1917	37,196	16	
1913	37,581			1918	30,204	327	$6,092.35
1914	32,756			1919	17,823	8	22,451.33
1915	30,681			1920	0	7,921	21,507.43
1916	38,388			1921	0	2,852	15,343.77

The sale of beer was discontinued October 29, 1919. The first sale of cereal beverage, dealcoholized beer, was November 27, 1917, under the name of "Pep." The first sale of soft drinks was July 1, 1918. After the eighteenth amendment became effective, the petitioner's sales of soft drinks and "near beer" declined, although the petitioner used as great effort to sell "near beer" and soft drinks as it had done theretofore.

Up to the time of the hearing the petitioner had used its best efforts to sell the premises, and the highest offer was $35,000 cash, made by the president of a paper company which owns the adjoining premises. About December 27, 1921, the petitioner sold to the paper company whose premises adjoined those of the petitioner 1.39 acres of the 3.53 acres of its land for $20,000. The land, which was sold free of buildings, had a frontage of 197 feet and depth varying from 282 to 334 feet.

55 The petitioner's lands, buildings, machinery, and equipment were at all times mentioned herein owned by it absolutely and without encumbrances.

The value of the property of the petitioner as determined by the city assessor of Niagara Falls for the assessment of property tax for the years indicated was as follows:

	Land value, exclusive of buildings	Full value of property less exemption, if any		Land value, exclusive of buildings	Full value of property less exemption, if any
1917	$47,990	$223,460	1921	$29,360	$129,760
1918	47,990	223,460		(18,630)	(18,630)
1919	47,990	183,460	1924	29,360	104,760
1920	29,360	164,830		(18,630)	(18,630)
	(18,630)	(18,630)			

The amounts shown in parenthesis for the years 1920, 1921, and 1924 represent the values placed by the assessor on the property sold by the petitioner in 1921 to the paper company.

The reduction in the values for the years 1919, 1921, and 1923 was made by the city assessor because the petitioner's buildings, which had been constructed and used for brewing beer, could no longer be used for that purpose on account of prohibition and because of the unsuitableness of the buildings for manufacturing purposes. Assessments on non-brewery property generally were increased during the same period.

The reduction in the value was not made entirely prior to the year 1923 for the reason that prior thereto the city assessor had not as thoroughly gone into the question of the value of the property as he had at that time.

When the petitioner ceased manufacturing beer on October 28, 1919, it abandoned the lower floor, consisting of storage space, in a building on its premises designated in the evidence as build-
56 ing No. 4. The space so abandoned had been used for the storage and aging of beer, but its use was not required in

making the beverage containing less than one-half of one per cent of alcohol by volume. The cost of building No. 4 to December 31, 1917, was $67,913.74, and the depreciation accrued to that date was $23,875.37, making a depreciated cost of $44,038.37. The cost of building No. 4 to March 1, 1913, was $67,913.74, and depreciation accrued to that date amounted to $16,538.70, making a depreciated cost of $51,375.04.

One of the petitioner's buildings, designated in the evidence as building No. 3, was divided into two parts, easterly and westerly. About 1917 the petitioner rebuilt the inside of the easterly part of the building and installed a storage cellar and new filtering and bottling machinery. The cost of building No. 3 to December 31, 1917, was $70,938.89, and the depreciation accrued to that date was $24,934.52, leaving a depreciated cost of $46,004.37. The cost of building No. 3 to March 1, 1913, was $53,083.13, and the depreciation accrued to that date was $13,088.46, leaving a depreciated cost of $39,994.67. The cost to December 31, 1917, of the machinery in building No. 3 was $27,453.09, and the depreciated cost at that date was $24,707.79. After October 28, 1919, and until about January, 1922, the easterly part of building No. 3, with the equipment therein, was used about once every two weeks in making "near beer," or cereal beverage, and aside from that it was not used for any other purpose. Prior to October 28, 1919, the easterly part of the building and the equipment therein were used about three or four times a week in making and bottling beer.

Inasmuch as the petitioner could not operate its business at a profit after prohibition, it dissolved under voluntary consent of the stockholders by certificate to such effect filed with the secretary of state of the State of New York on December 1, 1921, its affairs
57 in dissolution being administered by its directors as trustees in dissolution.

Under a lease dated January 31, 1922, and effective from January 15, 1922, the petitioner leased all its buildings, plant, and equipment, including its soft-drink equipment, under a lease running for a period of three months, renewable at three-month intervals at the option of the lessee and which lease at the time of the hearing was still in operation at an annual rental of $5,000 plus taxes, insurance, and repairs. This was the highest and only rental offered at any time to officers and agents of the petitioner for the property. The lessee was not a stockholder or director of the petitioner and had no financial connection with the petitioner at the time the lease was made. Although he was never a stockholder of the petitioner, he formerly had been its secretary, resigning in February, 1922, and a number of years prior thereto had been a director for one year.

The value of petitioner's machinery in 1918 and 1919 after prohibition became reasonably certain was not in excess of $10,475, which was less than its book value either on December 31, 1918, or

December 31, 1919, after deducting the amounts for obsolescence taken by the petitioner for the respective years.

At the end of 1918 and 1919 the petitioner's land had a value of about $46,000, whereas the buildings had a value of about $34,000. The value of the land and buildings at the end of the respective years was less than their book value after deducting for obsolescence the amounts taken by the petitioner for these years in its returns.

The difference between the value in 1918 and 1919 and depreciated cost of petitioner's machinery, buildings, and land at December 31, 1917, was due to the imminence and incidence of war-time and permanent prohibition legislation. There was no ma-
58 terial change in the value of land and buildings in the vicinity of those of the petitioner used for purposes other than brewing.

In making the cereal beverage containing less than one-half of one per cent of alcohol by volume manufactured and sold by the petitioner after October 28, 1919, the same machinery and the same process, except the dealcoholizing before bottling, was used as had been used in making beer. This cereal beverage had the same appearance as the beer manufactured by the petitioner prior to October 28, 1919, but did not resemble it in taste, nor did it have the same popularity.

In 1918 the petitioner sold certain property located at Main and Niagara Streets, Niagara Falls, New York, and the loss determined by the respondent was understated by $5,000 due to the respondent in his computation having overstated the amount of depreciation previously taken.

OPINION

TRAMMELL: The errors assigned in the original petition were that the respondent failed to allow the petitioner as deductions in computing its net income (1) "a reasonable allowance for the exhaustion, wear, and tear of property used in the trade or business of the taxpayer, including a reasonable allowance for obsolescence"; (2) "losses sustained during the taxable year and not compensated for by insurance or otherwise incurred in the trade or business of the taxpayer."

With respect to the first assignment of error it does not appear from the record that there is any controversy concerning deductions for the exhaustion, wear, and tear of the property, but only as to the allowance of deductions for obsolescence.

In its brief the petitioner states that the contention for an allowance of a deduction on account of the obsolescence of intan-
59 gible assets, including good will, is not pressed in view of the board's decisions following the case of Red Wing Malting Company v. Willcuts (15 Fed. (2d) 626). In view of the petitioner's statement and of our holding in Manhattan Brewing Co. (6 B. T. A. 952), we must hold that the petitioner is not entitled to

a deduction for either year on account of obsolescence of intangible property, including good will. With respect to the assignment of error relating to obsolescence there remains to be considered the question of whether the petitioner is entitled to the deductions taken by it for obsolescence of tangible property as set out in our findings of fact.

Prior to September 5, 1917, the petitioner's business was the manufacture, production, sale, and distribution of beer containing more than one-half of one per cent of alcohol by volume. In November, 1917, the petitioner began to make and sell dealcoholized or "near" beer. About the first of July, 1918, it began making and selling soft drinks. Since obsolescence is not claimed on assets used in the manufacture of soft drinks, no further consideration will be given to these. The petitioner continued to manufacture and sell these three products until October 28, 1919, when on account of war-time and permanent prohibition legislation and the ratification of the eighteenth amendment it ceased to manufacture beer. The petitioner continued until about the time of its dissolution in December, 1921, to manufacture and sell dealcoholized or "near" beer, using the same machinery and the same process that were used in the manufacture of beer with the exception of dealcoholization before bottling. Immediately after dissolution, the petitioner's plant was rented to a former officer and continued in use for making "near beer." The assets used in the manufacture and sale of beer were continued in use in the manufacture of "near beer," except that the lower
60 floor of building No. 4 was no longer used. In manufacturing "near beer" the easterly part of building No. 3, with the equipment therein, was used less frequently than in manufacturing beer.

We have heretofore considered the question of the allowance of deductions for obsolescence of tangible assets due to prohibition legislation where the assets were continued in use after prohibition became effective and have denied such deductions. (Yough Brewing Co., 4 B. T. A. 612; Star Brewing Co., Inc., 7 B. T. A. 377.) We think our decisions in those cases are applicable and controlling here.

With respect to building No. 4 the petitioner contends that since in 1919 it abandoned the lower floor therein it is entitled to a deduction for obsolescence of at least $17,125.01, representing one-third of the depreciated cost of the building on March 1, 1913, of $51,375.04. If we were disposed to hold that obsolescence were allowable on account of abandonment of a part of a building, we do not have sufficient evidence to determine whether the amount contended for by the petitioner is correct or what the allowance should be. The contention therefore must be denied.

The petitioner also contends that on account of the reduced use of the machinery in building No. 3, as well as the reduced use of the building itself from an average of four times a week to once every two weeks after it had ceased making beer, it is entitled to a deduction of obsolescence of $59,398.22. The petitioner determines

this amount by taking 84 per cent of $70,712.16, which was the total of the depreciated cost of $46,004.39 of the building and $24,707.79 of the machinery at December 31, 1917. This contention must be denied in view of our holding that a deduction may not be taken for obsolescence where the assets were continued in use in the business.

The second error assigned in the original petition is that the
61 respondent failed to allow deductions for losses sustained during the taxable year and not compensated for by insurance or otherwise incurred in the trade or business of the petitioner. With the exception of a loss to be considered presently, we are unable to tell from the record what losses, if any, this assignment of error relates to unless the petitioner intended to raise the issue that if the deductions taken for obsolescence on tangible property are not allowable as obsolescence, then the petitioner is entitled to deduct as losses the amounts representing the decline in value of property resulting from prohibiition legislation. While the evidence shows that the value of the petitioner's assets during the years involved in this proceeding experienced a great decline on account of prohibition legislation, yet they were continued in use during succeeding years. In George Wiedemann Brewing Co. et al. (9 B. T. A. 797) we had occasion to consider the question of the allowance as losses of deductions representing decreases in value of assets which were used in subsequent years and there held that such deductions are not allowable. We think our decision in that case is applicable here.

At the hearing the petitioner amended its petition to allege that the respondent in determining a loss from the sale of certain property in 1918 had understated the amount of the loss by $5,000 as a result of having determined that the petitioner had previously taken depreciation of $5,000 more than it actually had. Inasmuch as the respondent admitted the correctness of the petitioner's allegation, the petitioner is entitled to have its net income reduced by the amount of $5,000.

Judgment will be entered under rule 50.

Now, August 5, 1929, the foregoing findings of fact & opinion certified from the record as a true copy.

[SEAL.] B. D. GAMBLE,
Clerk, U. S. Board of Tax Appeals.

62 Before United States Board of Tax Appeals

[Title omitted.]

Motion to reopen case for further evidence

Filed Apr. 7, 1928

Niagara Falls Brewing Company and the other petitioners named in the petition for appeal, by Basil Robillard, their counsel, move

the board for an order reopening this cause for the submission of further evidence on behalf of the petitioners, as hereinafter set forth.

This cause was argued May 11th, 1927, at the close of the hearing thereupon. The appeal arose from the refusal of the commissioner to grant an allowance to the petitioners for obsolescence of tangible assets for the years 1918 and 1919. The assets upon which obsolescence was claimed were used in the business of brewing beer at Niagara Falls, New York. In proving the amount of such obsolescence petitioners were obliged to submit proof as to the salvage value of said assets after such obsolescence deduction was taken.

On January 10th, 1928, petitioners entered into a contract with one Alexander G. Landreth of Niagara Falls, New York, for the purchase and sale of all of the assets the obsolescence of which is claimed by petitioners in this cause. Said sale was consummated by
63 the delivery of a warranty deed from the petitioner, Niagara Falls Brewing Company, to said Alexander G. Landreth, together with a bill of sale covering said assets. Said sale was bona fide, and the purchase price was one hundred fifty thousand dollars ($150,000), payable fifty thousand dollars ($50,000) in cash and one hundred thousand dollars ($100,000) in first mortgage upon the assets sold. Said deed and mortgage have been recorded in the Niagara County clerk's office. There were no negotiations for said sale nor were the same contemplated at the time of the close of the hearing of this cause nor until December 23rd, 1927. Said sale further establishes the actual salvage value of the assets of petitioner, Niagara Falls Brewing Company, which is one of the issues in this cause, and the facts of the aforesaid sale and the amount received thereon are material upon said issue. Said facts were unknown to the petitioners at the time this cause was heard before the Board of Tax Appeals.

On or about February 29th, 1928, petitioners caused a stipulation of the facts concerning said sale to be signed by their counsel and forwarded to the general counsel for the Commissioner of Internal Revenue. Said general counsel has refused to sign the stipulation of said facts so submitted after conference between the office of said general counsel and Mr. Edward C. Gruen, C. P. A., on behalf of your petitioners, at Washington, D. C., March 30th, 1928.

No previous application has been made for an order reopening this cause for the reception of said evidence. Application for such an order has been delayed since February 8th, 1928, pending negotiations with the general counsel for the Commissioner of Internal Revenue for the stipulation of said facts, practically all of which are matters of public record in the County of Niagara.

64 Wherefore your petitioners move for an order of this Board of Tax Appeals reopening this cause for the reception of said

evidence upon the salvage value of the assets considered herein and that your petitioners may have such other and further relief as to the board may seem just.

Dated April 5, 1928.

Respectfully submitted.

BASIL ROBILLARD,
Counsel for Petitioners.

Office & P. O. address, 425–443 Gluck Building, Niagara Falls, New York.

Now, August 5, 1929, the foregoing motion to reopen case certified from the record as a true copy.

[SEAL.] B. D. GAMBLE,
Clerk, U. S. Board of Tax Appeals.

65 Before United States Board of Tax Appeals

Excerpt from testimony re motion to reopen case

The MEMBER. I am inclined to think that this sale occurring so many years after the year involved is so remote from the transaction which gave rise to this tax liability that it would have very little probative value. There are so many things that intervene that might make the sales price greater or less than the value as shown already by the testimony in the case, and therefore it would probably have no probative value, and that being true, the motion to reopen the case for the taking of further testimony will be denied.

(Excerpt from testimony on motion to reopen case.)

Now, August 5, 1929, the foregoing excerpt from testimony re motion to reopen case certified from the record as a true copy.

[SEAL.] B. D. GAMBLE,
Clerk, U. S. Board of Tax Appeals.

66 Before United States Board of Tax Appeals

Minutes of proceedings on motion to reopen case

Date 4–19–28. Niagara Falls Brewing Co. et al. Docket No. 7952. Assigned to Trammell.

Counsel: For petitioner, E. Robillard; for respondent, M. E. McDowell. Stenographic reporter, Moore.

Ordered: Board.

On motion to reopen case for further evidence and also motion for extension of time to file brief. Motion to reopen case denied and 30 days additional time given for briefs.

Now, August 5, 1929, the foregoing minutes of proceedings re motion to reopen case certified from the record as a true copy.

[SEAL.] B. D. GAMBLE,
Clerk, U. S. Board of Tax Appeals.

67 Before United States Board of Tax Appeals

[Title omitted.]

Petition to have case reviewed by entire Board.

Filed Nov. 14, 1928.

To the Honorable the Board of Tax Appeals:

The undersigned, Niagara Falls Brewing Company and others, petitioners herein, respectfully show to this honorable board:

1. That the decision in this cause was promulgated under the above docket number October 16, 1928, and denied to your petitioners the right to deduct from the net income of the petitioner Niagara Falls Brewing Company, for the year 1918 and for the year 1919 certain amounts representing the obsolescence of tangible personal property of said petitioner in computing the income and excess profit tax of said petitioner.

2. That the opinion of the Board of Tax Appeals rendered upon the decision of this cause consists of seventeen typewritten
68 pages of which approximately twelve pages are devoted to findings of fact substantially in accordance with the contentions of the petitioners with the exception of the contentions of the petitioners that parts of various buildings of the petitioners had been abandoned.

3. That the opinion of the board contains findings that the cost or market value as of March 1st, 1913, of the assets of the petitioners are as shown by the proof of the petitioners and as claimed in petitioners' request to find, and that there are no findings in the opinion or findings of fact contrary to the contentions of the petitioners with respect to the salvage value of the said property of the petitioners upon which obsolescence was claimed.

4. That the Board of Tax Appeals has in various decisions allowed to other petitioners engaged in this business or a similar business deductions for obsolescence of tangible assets, which decisions are cited upon page 40 of the petitioners' brief.

5. That the Board of Tax Appeals in the decision of this cause refuses to allow to the petitioners deduction for obsolescence of tangible assets upon the ground that the tangible assets upon which the deduction for obsolescence is claimed were not abandoned by the petitioners. That said decision has failed to take into consideration the fact that article 143 of Regulation 45, which is enforced by the decision, is contrary to the provisions of section 234 of the income tax act of 1918, in that the said article of the regulation requires an abandonment of the assets upon which the obsolescence deduction is taken, whereas no such requirement for abandonment is contained

in said section of the statute. By point II of the petitioners' brief herein petitioners showed that under the decisions of the Supreme Court of the United States it has been consistently and frequently held that regulations of heads of departments such as the Commissioner of Internal Revenue are void and of no force and effect in so far as they attempt to add by regulation to the taxation burden imposed by act of Congress.

6. That the decision of the board fails to take into consideration or to discuss in the opinion the validity or invalidity of the article of regulations referred to and fails to give weight to the various decisions of the United States courts, including the United States Supreme Court, holding that the regulations of the Commissioner of Internal Revenue in so far as they added additional burdens to a tax statute were void and of no effect. That the said cases of the United States Supreme Court are cited upon page 45 of the printed brief for petitioners filed herein.

7. That aside from the failure of the board to find that petitioner abandoned the assets upon which the obsolescence deduction was claimed the board by its decision has made sufficient findings to entitle the petitioners to the obsolescence deduction claimed.

Wherefore the petitioners pray for an order of the board that this cause shall be reviewed by the entire Board of Tax Appeals, that petitioners may have leave to argue this cause before the entire Board of Tax Appeals, setting the date for such review, and that petitioners may have such other and further relief as to the board may seem just.

Dated, November 12, 1928.

Respectfully submitted.

BASIL ROBILLARD,
Attorney for Petitioners.

Office and post office address, 425-443 Gluck Building, Niagara Falls, N. Y.

[Duly sworn to by George F. Nye; jurat omitted in printing.]

Denied, Nov. 15, 1928.

(Signed) BENJ. H. LITTLETON,
Chairman.

Now, August 5, 1929, the foregoing motion to have case reviewed by entire board certified from the record as a true copy.

[SEAL.] B. D. GAMBLE,
Clerk, U. S. Board of Tax Appeals.

71 Before United States Board of Tax Appeals

NIAGARA FALLS BREWING COMPANY AND PAUL Schoellkopf, Charles E. Haeberle, Fred H. Krull, Edson P. Pfohl, Albert T. Mayle, Frederick Chormann, Rudolf V. Rose and George F. Nye, as Directors and Trustees in Dissolution, petitioners v. COMMISSIONER OF INTERNAL REVENUE, respondent	Docket No. 7052

Order of redetermination

Pursuant to the findings of fact and opinion of the board promulgated October 16, 1928, the respondent in the above entitled proceeding filed notice of settlement with the board on December 5, 1928. Copy of said notice having been duly served on the petitioners, together with notice of hearing, and the case having been called for settlement on January 14, 1929, at which time no objection to the proposed settlement was offered, it is

Ordered and decided upon redetermination that for 1918 the correct tax liability is $18,561.17 that there has been assessed $20,975.05 leaving an unpaid assessment to be abated of $2,413.88, and that for 1919 there is a deficiency of $5,013.65 which has been assessed.

[SEAL.] (Signed) CHARLES M. TRAMMELL,
Member, United States Board of Tax Appeals.

Entered, Jan. 18, 1929.

Now, August 5, 1929, the foregoing order of redetermination certified from the record as a true copy.

B. D. GAMBLE,
Clerk, U. S. Board of Tax Appeals.

72 In United States Circuit Court of Appeals

[Title omitted.]

Petition for the review of decision of the United States Board of Tax Appeals

Filed July 16, 1929

To the honorable the Judge of the United States Circuit Court of Appeals for the Second Circuit:

The petitioners in support of this their petition filed in pursuance of the provisions of section 1001 of the act of Congress approved February 26, 1926, entitled "The revenue act of 1926," and the acts amendatory thereof and supplemental thereto, for the review

of the decision of the United States Board of Tax Appeals rendered on January 18, 1929, approving a deficiency in income and excess profits taxes of the petitioner Niagara Falls Brewing Com-
73 pany for the calendar year 1918 in the amount of eighteen thousand five hundred sixty-one dollars and seventeen cents ($18,561.17), and for the calendar year 1919 in the amount of five thousand thirteen dollars and sixty-five cents ($5,013.65), respectfully show to this honorable court as follows:

I

STATEMENT OF THE NATURE OF THE CONTROVERSY

1. The appellant Niagara Falls Brewing Company at the times hereinafter mentioned until December 1, 1921, was a corporation of the State of New York which on December 1, 1921, was dissolved by a voluntary consent of its stockholders and the other appellants have been (with Frederick Chormann and Rudolph V. Rosa, since deceased), and now are, directors of said corporation acting as trustees thereof in dissolution.

2. This corporation appellant duly filed its income tax and excess profits taxes returns for the year 1918 showing that no tax was due from said appellant for that year, and for the year 1919 showing that one hundred thirty-eight dollars and ninety-two cents ($138.92) tax was due from the appellant for that year on account of income and excess profits taxes. Under and pursuant to the provisions of section 274 (d) of the revenue act of 1924 the appellee as Commissioner of Internal Revenue assessed against said appellant additional income and excess profits taxes for the year 1918 in the sum of twenty thousand nine hundred seventy-five dollars and five cents ($20,975.05) and for the year 1919 in the sum of five thousand one hundred thirty-seven dollars and fifty-seven cents ($5,137.57) and caused to be served upon said appellant notices in demand for the payment of said additional assessments. Said appellant on January
15, 1925, duly executed and filed claim in abatement of said
74 additional assessments with the collector of internal revenue for the twenty-eighth New York district, accompanied by a bond in the sum of thirty-five thousand dollars ($35,000.00) which is still subsisting and outstanding conditioned for the payment of said assessments. Under date of August 13, 1925, said claim for abatement was rejected by appellee and said appellants thereafter duly filed with the United States Board of Tax Appeals their petition for appeal therefrom, which was docketed by said Board of Tax Appeals under docket No. 7952.

3. Said additional assessment was caused by the disallowance by said Commissioner of Internal Revenue, appellee, of deductions in the computation of the income of said appellant on account of obsolescence of the real property and machinery of said appellant during the year 1918 amounting to one hundred ten thousand forty-seven dollars and fifty-two cents ($110,047.52), and to fifty-seven

thousand one hundred thirty-nine dollars and ninety-nine cents ($57,139.99) for the year 1919 actually written off upon the books of account of the taxpayer on account of the imminence, incidence, and promulgation of prohibition legislation and the eighteenth amendment to the Constitution of the United States.

4. Thereafter the appellants by motion dated December 10, 1925, moved to amend their petition for appeal in reference to the computation of invested capital of said appellant under the decision of said board in the appeal of Guaranty Construction Company, decided after the petition in this cause was filed. Said motion was granted December 15, 1925, by said board and the appellee on January 1, 1926, filed his answer to said amended petition. Upon the issue thus joined proof was submitted by the appellants, together with a stipulation of facts, and the cause was argued before said Board of Tax Appeals May 11, 1927.

75 5. Thereafter on April 5, 1928, appellants filed their motion with said Board of Tax Appeals to reopen the cause to permit the appellants to submit further proof to show the actual amount realized upon the sale on January 10, 1928, of the assets of said appellant upon which the obsolescence was claimed, for a sum less than the book value thereof after said deductions for obsolescence, but said Board of Tax Appeals after hearing said motion denied the said motion, to which the appellants took an exception upon the record.

6. On October 16, 1928, said United States Board of Tax Appeals rendered and promulgated its decison of said cause based upon findings of fact, together with an opinion sustaining the appellee in his refusal to allow said deductions for obsolescence, and in his assessment of additional income and excess profits taxes against the appellant, Niagara Falls Brewing Company, for the years 1918 and 1919, with the exception of income and excess profits taxes upon five thousand dollars ($5,000.00) by which the income of the said appellant for the year 1918 had been overstated; and on November 14, 1928, the appellants duly filed their petition verified November 12, 1928, for an order that the cause be reviewed by the entire United States Board of Tax Appeals, which petiton was denied November 15, 1928, by said United States Board of Tax Appeals and Benjamin H. Littleton as chairman thereof.

7. On January 18, 1929, said board entered its final order of redetermination approving a deficiency of income and excess profits taxes of said appellant for the year 1918 of eighteen thousand five hundred sixty-one dollars and seventeen cents ($18,561.17) and for the year 1919 of five thousand thirteen dollars and sixty-five cents ($5,013.63).

II

76

DESIGNATION OF COURT OF REVIEW

1. Petitioner is a corporation of the State of NewYork with its principal place of business in the city of Niagara Falls, New York, and being aggrieved by the said findings of fact, opinion, decision,

and order, seeks a review thereof in accordance with the provisions of the revenue act of 1926 and the acts amendatory thereof and supplemental thereto by the United States Circuit Court of Appeals for the second Circuit, within which circuit is located the office of the Collector of Internal Revenue for the twenty-eighth New York district with whom the appellant made and filed its returns of income and excess profits taxes.

III

ASSIGNMENT OF ERRORS

The petitioners as a basis for review make the following assignments of error:

1. The Board of Tax Appeals erred in denying to the petitioners a deduction and the right to deduct in the computation of the income of the petitioner, Niagara Falls Brewing Company, for the calendar year of 1918, of the sum of $110,047.52, on account of the obsolescence of the real property and machinery of said petitioner during said calendar year, and in denying to said petitioners the deduction and the right to deduct in the computation of income of said petitioner the sum of $57,139.99, from its income for the calendar year of 1919, on account of such obsolescence of the real property and machinery of said petitioner during said year.

2. That the Board of Tax Appeals erred in holding that
77 the Commissioner of Internal Revenue properly refused said deductions from the income of said petitioner for said year on account of such obsolescence.

3. The Board of Tax Appeals erred in holding that the petitioners were not entitled to said deduction from the income of said petitioner for said calendar years on the ground that said petitioner had not abandoned the real property and machinery upon which said obsolescence deductions were taken.

4. The Board of Tax Appeals erred in holding that the petitioner by engaging in the business of making and selling a cereal beverage of alcoholic content of less than one-half of one per cent by volume continued in the same business which it had conducted prior to the incidence and promulgation of war-time prohibition, and of the eighteenth amendment to the Constitution of the United States and the statutes enacted in enforcement thereof.

5. The Board of Tax Appeals erred in holding that the petitioner, Niagara Falls Brewing Company, did not abandon the assets upon which said obsolescence deduction was taken.

6. The Board of Tax Appeals erred in holding that the said petitioner did not abandon one-third of its storage building designated in the testimony as building #4.

7. The Board of Tax Appeals erred in holding that said petitioner did not abandon at least one-half of its bottling building, designated in the testimony as building #3, to the extent of 84% of the use thereof.

8. The Board of Tax Appeals erred in holding that an abandonment of any tangible assets was necessary to entitle the petitioner, Niagara Falls Brewing Company, to a deduction against its income for said taxable years for and on account of the obsolescence of said tangible assets.

9. The Board of Appeals erred in holding that the peti-
78 tioner, Niagara Falls Brewing Company, did not sustain during the taxable year 1918, by reason of the incidence and promulgation of war-time prohibition, the eighteenth amendment to the Constitution of the United States, and the statutes in enforcemen thereof, a loss uncompensated by insurance or otherwise, and that the said petitioner did not sustain during the calendar year of 1919 a similar loss by reason of the same tax.

10. The Board of Tax Appeals erred in denying to the petitioner, Niagara Falls Brewing Company, a deduction from its income for the calandar year 1918, in the sum of $110,047.52, on account of the loss sustained during said calendar year due to the incidence and promulgation of war-time prohibition, the eighteenth amendment to the Constitution of the United States and the statutes in enforcement thereof, and uncompensated by insurance or otherwise, and in denying to said petitioner a similar deduction from its income for the year 1919, in the amount of $57,139.99, on account of such a loss similarly sustained during said calendar year.

11. The Board of Tax Appeals erred in denying an obsolescence deduction from the income of the said petitioner, Niagara Falls Brewing Company, for the calendar years 1918 and 1919, in the amounts above stated, upon the ground that the property upon which the obsolescence deduction was based had not become entirely obsolete.

12. The Board of Tax Appeals erred in rendering decision for the respondent.

Wherefore your petitioners pray that this honorable court may review such findings, decision, opinion, and order and reverse and set aside the same, and that the clerk of the United States Board of Tax Appeals be directed to transmit and deliver to the clerk of this court certified copies of all and every of the documents necessary and material to the presentation and consideration of the foregoing
79 petition for review, and as required by the rules of said court and the statutes made and provided.

And your petitioners will ever duly pray.

THE NIAGARA FALLS BREWING COMPANY.
By GEORGE F. NYE, *President.*

BASIL ROBILLARD,
Attorney for petitioners,
430 Gluck Building, Niagara Falls, N. Y.

[*Duly sworn to by George F. Nye; jurat ommitted in printing.*]

Now, August 5, 1929, the foregoing petition for review certified from the record as a true copy.

B. D. GAMBLE,
Clerk, U. S. Board of Tax Appeals.

80 In United States Circuit Court of Appeals

[Title omitted.]

Præcipe for record

Filed July 17, 1929

To the Clerk of the United States Board of Tax Appeals:

Will you please prepare and within sixty (60) days from the date of filing of petition for review in the above-entitled cause place with the clerk of United States Circuit Court of Appeals certified copies of the following documents:

1. Docket entries of proceedings before the United States Board of Tax Appeals in the case above entitled.

2. The pleadings of the board before the United States Board of Tax Appeals in said cause.

3. The findings of fact, opinion, and decision of the United States Board of Tax Appeals therein.

4. The motion of the above-named petitioners dated April
81 5th, 1928, with the accompanying petitions and accompanying papers whereby the petitioners sought leave to reopen this cause.

5. The decision of the Board of Tax Appeals upon said last named petition.

6. The petition for review of this cause by the entire Board of Tax Appeals.

7. The order determining the deficiency herein.

8. The petition for appeal herein to United States Circuit Court of Appeals for the Second Circuit.

The foregoing to be prepared, certified, and transmitted as required by law and the rules of United States Circuit Court of Appeals for the Second Circuit.

BASIL ROBILLARD.

Basil Robillard, attorney for the petitioners, 430 Gluck Building, Niagara Falls, N. Y.

JULY 13, 1929.

Now, August 5, 1929, the foregoing præcipe certified from the record as a true copy.

[SEAL.]

B. D. GAMBLE,
Clerk, U. S. Board of Tax Appeals.

82 In United States Circuit Court of Appeals for the Second Circuit

No. 144—October term, 1929

Argued November 22, 1929. Decided December 9, 1929

NIAGARA FALLS BREWING COMPANY AND Paul A. Schoellkopf, Chas. E. Haeberle, Fred H. Krull, Edson P. Pfohl, Albert T. Mayle, Frederick Chormann, Rudolph V. Rose and George F. Nye, as Directors of said Company and Trustees thereof in dissolution, petitioners v. COMMISSIONER OF INTERNAL REVENUE, respondent	Appeal from the United States Board of Tax Appeals Before MANTON, L. HAND, and MACK, Circuit Judges

Petition to review a determination of the U. S. Board of Tax Appeals. 13 B. T. A. 1040. Order reversed.

Basil Robillard, of Niagara Falls, N. Y., for appellants.

J. Louis Monarch and Norman D. Keller, Sp. Assts. Atty. Gen. (C. M. Charest, Gen. Counsel, Bureau of Internal Revenue, and John McC. Hudson, sp. atty., Bureau of Internal Revenue, both of Washington, D. C., of counsel), for respondent.

Opinion

MANTON, Circuit Judge: The petitioner manufactured beer prior to the advent of the national prohibition. In reporting for income and profit taxes for the years 1918 and 1919, it charged off obsolescence as a loss because its property, consisting of land, buildings, and machinery, became obsolete. On redetermination, it has been directed to pay the sum of $18,561.17 for 1918 and $5,013.65 for 1919. Feeling aggrieved by this order of redetermination, it has taken this appeal.

The facts found by the board have been acquiesced in by both petitioner and respondent. They may be stated briefly as follows:

The petitioner, a New York corporation, manufactured beer prior to the enactment of the eighteenth amendment to the Constitution and the acts of Congress (27 U. S. C. A.) passed in the enforcement thereof. Its business and good will were all created by the manufacture and sale of this beverage, which is now forbidden to be manufactured and sold. It purchased its buildings and equipment in 1902, and thereafter constructed some new buildings, purchased and installed additional machinery, fixtures, and equipment, but these were especially constructed, designed, and adapted for the business of manufacturing beer and were not available or readily adaptable to

other uses. About July 1, 1918, the petitioner commenced to manufacture soft drinks in a separate building, with machinery distinct from that used in the manufacture of beer or cereal beverages, and kept separate accounts therefor on its books. It was obliged to discontinue the sale of beer, malt, and spirituous liquors after the forbidden time, and ceased doing so. It made near beer after it discontinued this manufacture of beer, but no part of the obsolescence or extraordinary depreciation taken by the petitioner for the years 1918 or 1919 was computed upon or taken on account of the depreciation of the buildings, machinery, and equipment used for the manufacture of soft drinks other than dealcoholized beer. The
83 investment in equipment for the manufacture of soft drinks other than dealcoholized beer and the depreciation thereof was small for the years in question.

Prior to March 1, 1913, the plant and buildings were found by the board to have a value equal to the amount set up on the books of the petitioner of $476,265.16 on December 31, 1917. The total cost was $635,800.93; the accrued depreciation, $158,746.33. The book cost, found to be the true value by the board, was as to fixed assets on December 31, 1918, and December 31, 1919, respectively, $603,275.38 and $609,543.29, and there was charged off for obsolescence in the year 1918, $110,047.52, and for the year 1919, $57,139.99. It is these two items which the board has disallowed in fixing the income for each year. The rate of depreciation was fixed by the taxpayer. The obsolescence was taken only on the property which was used to brew beer. The deductions for obsolescence represented the amount necessary to be written off the assets to bring them down to an amount which the petitioners' directors thought could be realized at a forced or liquidation sale after the imminent prohibition legislation should become effective. The amount of deduction was determined after inquiry by the president of the petitioner as to what brewing machinery would bring in the case of prohibition, and deductions for depreciation and obsolescence were approved by the board of directors and the stockholders in the years charged off. The amount written off in the year 1919 was based, among other things, on the fact that the assets of a similarly situated brewing company in the same city had taken greater deductions for obsolescence than the petitioner and had sold in 1919 only a fractional part of the amount at which the assets remained on the books.

Other conditions found were that the petitioner had to curtail the brewing of beer considerably more than theretofore, and that, in the event that it attempted to dispose of its machinery, it could not find a market because of so much of that kind of machinery was being offered for sale. It entirely abandoned the manufacture and sale of beer in 1919. The petitioner considered selling or converting its building and machinery into plants for various other manufacturing and commercial purposes, but they could find no use for the building and machinery. The buildings were damp, the floor levels were un-

even, they had no elevators, few openings for light, and were not readily adaptable for storage, manufacturing, or industrial purposes. The buildings were zoned, under the city zoning law, in an industrial or manufacturing zone. Much of the brewing machinery could not be removed from the buildings without tearing out the walls of the building or dismantling the machinery, and some of the machinery could not be dismantled without tearing out a side of the building. Having used its best efforts to sell the premises, the highest offer received was $35,000 cash, made by a paper company, which owned adjoining premises. Later the petitioner sold that portion of its land which was free from buildings for $20,000. The property was free of incumbrances.

The city assessor reduced the assessments very considerably, because it could no longer be used for brewing beer and was unsuitable as a building for other manufacturing purposes, although in the same locality other property used for nonbrewing purposes was generally increased during the same period. When the taxpayer ceased manufacturing beer on October 28, 1919, it abandoned the lower floor, consisting of storage space in the building designated as No. 4. Space so abandoned had been used for storing and aging of beer. The cost of building No. 4 on December 31, 1917, was $67,913.74, and the depreciation accruing to that date was $23,875.37, making a total depreciation of $44,038.37. The cost of building No. 4 on March 1, 1913, was $67,913.74, and the depreciation accrued to that date amounted to $16,538.70, making a depreciation cost of $51,375.04. Building No. 3 was divided into two parts—easterly and westerly—and it was depreciated in 1917, the petitioner rebuilding inside of the easterly part of said building and reconstructing the storage cellar and new filtering and bottling machinery. The cost of this building on December 31, 1917, was $70,938.89, and the depreciation occurring to that date was $24,934.52, leaving a depreciated cost of $46,004.37. The cost of the building No. 3 on March 1, 1913, was $53,083.13, and the depreciation occurring to that date was $13,088.46, leaving a depreciated cost of $39,994.67. The cost on December 31, 1917, of the machinery and plant No. 3 was $27,453.09, and the depreciated cost of that date was $24,707.79. After October 28, 1919, and until January, 1922, the easterly part of the building No. 3, with the equipment therein, was used but once or twice a week making near beer, and aside from this it was not used for any other purpose.

84 Prior to October, 1928, the easterly part of the building and equipment therein was used three or four times a week in making and bottling beer.

The taxpayer was dissolved as a corporation December 1, 1921, and its affairs of dissolution were administered by the directors as trustees in dissolution. Thereafter the building was leased for three months at an annual rental of $5,000, plus taxes, insurance, and repairs, to manufacture soft drinks. The lessee had no relation to the taxpayer, except that of tenant. The value of the machinery in

1918–1919, after prohibition became reasonably certain, was found to be not in excess of $10,475. At the end of 1918–1919 the land value was found to be $46,000 and the buildings $34,000. These amounts were less than the book values, after deducting for obsolescence the amount taken out by the petitioners for these years in its returns.

It is conceded that the difference in value in 1918 and 1919, and the depreciation cost of petitioner's machinery, buildings, and land on December 31, 1917, was due to incidence of war-time and permanent prohibition. There was no material change in the value of land and buildings in the vicinity of those of the petitioner used for purposes other than brewing.

On these facts the question presented was whether there was a deductible loss with respect to the property in 1918 and 1919 for obsolescence. Section 324 of the revenue act of 1918 (40 Stat. 1057, 1077) provided:

"(a) That in computing the net income of a corporation subject to the tax imposed by section 230 there shall be allowed as deductions: * * * (7) A reasonable allowance for the exhaustion, wear and tear of property used in the trade or business, including a reasonable allowance for obsolescence; * * *"

The Treasury Department in its regulations provided in Regulation 45 as follows:

"Art. 143. *Loss of useful value.*—When through some change in business conditions the usefulness in the business of some or all of the capital assets is suddenly terminated so that the taxpayer discontinues the business or discards such assets permanently from use in the business he may claim as a loss for the year in which he takes such action the difference between the cost or the fair market value as of March 1, 1913, of any asset so discarded (less any depreciation allowances) and its salvage value remaining. This exception to the rule requiring a sale or other disposition of property in order to establish a loss requires proof of some unforeseen cause by reason of which the property must be prematurely discarded, as, for example, where machinery or other property must be replaced by a new invention, or where an increase in the cost of or other change in the manufacture of any product makes it necessary to abandon such manufacture to which special machinery is exclusively devoted, or where new legislation directly or indirectly makes the continued profitable use of the property impossible. This exception does not extend to a case where the useful life of property terminates solely as a result of those gradual processes for which depreciation allowances are authorized. It does not apply to inventories or to other than capital assets. The exception applies to buildings only when they are permanently abandoned or permanently devoted to a radically different use, and to machinery only when its use as such is permanently abandoned. Any loss to be deductible under this exception must be charged off on the books and fully explained in returns of income. But see articles 181–188."

If this regulation provides an additional condition which must be satisfied before obsolescence deduction can be taken—that is, that the property must first be abandoned and that its usefulness must be terminated—the taxpayer would be deprived of the privilege of taking deductions of a reasonable allowance for obsolescence, unless he first abandons the assets. But this regulation does not apply. The statute provides for obsolescence, and not for obsoleteness. Obsolescence may and does occur, resulting in an estate more obsolete, when less used or more neglected, without forthwith rendering it entirely obsolete, useless, and fit only to be abandoned. "Obsolescence" is defined by Webster's Dictionary "as a state of becoming obsolete," "as no longer in use, disused, neglected"; and the Standard Dictionary defines "obolescence" as a condition or process of gradually falling into disuse.

The existence of obsolescence in the earlier acts was recognized, but it was held not to be included in terms "depreciation," "exhaustion," "wear or tear," and obsolescence was permitted only when it had ripened into obsoleteness. This resulted in throwing the total deduction for obsolescence, as distinguished from depreciation, into one year. Congress then provided for the recognition of obsolescence as a progressive process, as distinguished from obsoleteness,
85 which was an accomplished status. If there be obsolescence, without obsoleteness, it is clear that Congress intended to permit the deduction of the amount for obsolescence without abandonment of the assets. To impose another condition, the Treasury Department went beyond the statute. It created an additional burden upon the taxpayer, not provided for by the statute, and is unlawful. (International R. R. Co. v. Davidson, 257 U. S. 506, 42 S. Ct. 179, 66 L. Ed. 341; United States v. George, 228 U. S. 14, 33 S. Ct. 412, 57 L. Ed. 712; Williamson v. United States, 207 U. S. 425, 28 S. Ct. 163, 52 L. Ed. 278.) Moreover there was an abandonment of the business, the use of the machinery and of the buildings, except for the short period when a portion thereof was used for the manufacture of soft drinks.

We said in Haberle Crystal Springs Brewing Co. v. Clarke (30 F. (2d) 219, 220), where a claim of obsolescence for good will was made: "A brewery may fairly be regarded as obsolete after prohibition, and as subject to obsolescence during the period between the date when such legislation became certain and the date when it went into effect. The taxing authorities do not deny that legislation which shortens the useful life of tangible assets entitles the taxpayer to an allowance for obsolescence under the 1918 act. (Appeal of Manhattan Brewing Co., 6 B. T. A. 952, which allowed obsolescence of tangibles but not of good will, because of the imminence of prohibition.)"

Upon the conceded facts here, the amounts claimed for obsolescence were justified and should have been allowed.

Determination reversed.

86 In United States Circuit Court of Appeals, Second Circuit

NIAGARA FALLS BREWING COMPANY ET AL., PETITIONERS

v.

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

Appeal from the United States Board of Tax Appeals

Decree

Filed Dec. 16, 1929

This cause came on to be heard on the transcript of record from the United States Board of Tax Appeals and was argued by counsel.

On consideration whereof it is now hereby ordered, adjudged, and decreed that the order of said United States Board of Tax Appeals be, and it hereby is, reversed.

It is further ordered that a mandate issue to the said board in accordance with this decree.

WM. PARKIN, *Clerk.*

87 [File endorsement omitted.]

88 [Clerk's certificate to foregoing transcript omitted in printing.]

SUPREME COURT OF THE UNITED STATES

Order allowing certiorari

Filed April 28, 1930

The petition herein for a writ of certiorari to the United States Circuit Court of Appeals for the Second Circuit is granted. And it is further ordered that the duly certified copy of the transcript of the proceedings below which accompanied the petition shall be treated as though filed in response to such writ.

[Endorsement on cover:] File No. 34872. U. S. Circuit Court of Appeals, Second Circuit. Term No. 741. Robert H. Lucas, Commissioner of Internal Revenue, petitioner, vs. Niagara Falls Brewing Company, and Paul A. Schoellkopf, Charles E. Haeberle, et al., etc. Petition for writ of certiorari and exhibit thereto. Filed March 15, 1930. File No. 34872.

U. S. GOVERNMENT PRINTING OFFICE: 1930

FILE COPY

FILED
MAR 15 1930
CHARLES ELMORE CROPLEY

No. 64

In the Supreme Court of the United States

OCTOBER TERM, 1929

ROBERT H. LUCAS, COMMISSIONER OF INTERNAL REVENUE, PETITIONER

v.

NIAGARA FALLS BREWING COMPANY, AND PAUL A. SCHOELLKOPF, CHAS. E. HAEBERLE, FRED H. KRULL, EDSON P. PFOHL, ALBERT T. MAYLE, FREDERICK CHORMANN, RUDOLF V. ROSE, AND GEORGE F. NYE, AS DIRECTORS OF SAID COMPANY AND TRUSTEES THEREOF IN DISSOLUTION.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT, AND BRIEF IN SUPPORT THEREOF

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CITATIONS

Clarke v. *Haberle Brewing Co.*, 280 U. S. 384	6, 10, 11
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101439—30

In the Supreme Court of the United States

OCTOBER TERM, 1929

No. ——

ROBERT H. LUCAS, COMMISSIONER OF INTERNAL REVENUE, petitioner

v.

NIAGARA FALLS BREWING COMPANY, AND PAUL A. SCHOELLKOPF, CHAS. E. HAEBERLE, FRED H. KRULL, EDSON P. PFOHL, ALBERT T. MAYLE, FREDERICK CHORMANN, RUDOLF V. ROSE, AND GEORGE F. NYE, as Directors of said Company and Trustees thereof in dissolution.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT, AND BRIEF IN SUPPORT THEREOF

PETITION

The Attorney General on behalf of the Commissioner of Internal Revenue prays that a writ of certiorari issue to review the judgment of the United States Circuit Court of Appeals for the Second Circuit entered in the above cause on December 16, 1929, reversing the decision of the United States Board of Tax Appeals.

STATEMENT

This case reached the Circuit Court of Appeals on the petition of respondents, Niagara Falls Brewing Company, et al., for a review of the decision of the Board of Tax Appeals determining deficiencies in respondents' income and profits taxes for the years 1918 and 1919 in the respective amounts of $18,561.17 and $5,013.65. (R. 71.)

The material facts are not in dispute and may be briefly stated as follows (R. 47–58):

Prior to national prohibition, the taxpayer was engaged in manufacturing and selling beer. Its business and good will were created by such manufacture and sale. At the time of its organization in 1902, the taxpayer acquired the buildings and equipment of a predecessor brewing company and thereafter it constructed new buildings and installed additional machinery and equipment which were specially constructed and designed for the manufacture of beer and were not available or readily adaptable for other uses. In 1917 the taxpayer began the manufacture and sale of dealcoholized beer, known as "near beer," in the production of which the same machinery and the same processes were used as were employed in making alcoholic beer. In 1919 the manufacture and sale of beer was discontinued and entirely abandoned because of national prohibition, but "near beer" was thereafter produced and sold by the taxpayer in order to see if the plant could be profitably operated. Sales of this beverage, however, declined after the effective

date of the Eighteenth Amendment, although the taxpayer did not lessen to any degree its efforts to make sales of the product.

The taxpayer, upon abandonment of the manufacture and sale of beer in 1919, considered adapting its plant to other manufacturing and commercial purposes, but no other use could be found for the plant because the construction and condition of the buildings and machinery rendered them unsuitable for and not readily adaptable to other uses, and the best offer obtainable by the taxpayer for the purchase of the property was $35,000 in cash made by the owner of adjoining premises. When the sale of beer was discontinued in October, 1919, the taxpayer abandoned the lower floor of one of its buildings which had been devoted to storing and aging beer. Thereafter one-half of another building, with the equipment therein, which had been used three or four times a week in manufacturing beer was used only about once every two weeks in making "near beer." In December, 1921, the taxpayer dissolved as a corporation because of its inability to operate the business at a profit after prohibition and in January, 1922, the plant was leased for three months, renewable at the option of the lessee, at an annual rental of $5,000 p[illegible] taxes, insurance, and repairs, which was the highest rental offered at any time.

The depreciated cost of the buildings, machinery, and equipment used in the manufacture of beer was $300,968.86 on March 1, 1913, and $377,054.60 on

December 31, 1917. These amounts also represented the fair values of the properties on the same dates. The net depreciated book cost of the same properties at December 31, 1918, was $193,918.95 and at December 31, 1919, was $129,814.16. The value of the machinery in 1918 and 1919 after prohibition became reasonably certain was not in excess of $10,475, while the value of the buildings at the same time was about $34,000.

The taxpayer charged against its earnings and deducted on its income-tax returns the sum of $110,047.52 in 1918 and the sum of $57,139.99 in 1919 for obsolescence of its buildings, machinery, and equipment used in the manufacture and sale of beer. These amounts so deducted represented the charges considered necessary to bring the assets down to an amount realizable upon a forced or liquidation sale after prohibition, and were determined upon consideration of what similar property could be and had been sold for and in the light of the fact that the brewing of beer had been necessarily curtailed more than theretofore, and the further fact that no market was available for the sale of machinery and equipment of that kind. The value of all the property used in the manufacture and sale of beer at the end of 1918 and 1919 was less than its depreciated cost or book value after deducting the amounts charged off for obsolescence of such property during those years. The difference between the value in 1918 and 1919 and the depreciated cost of the petitioner's ma-

chinery and buildings at December 31, 1917, was due to the imminence and incidence of war-time and permanent prohibition legislation.

The Commissioner disallowed the deductions claimed for obsolescence on the ground that the taxpayer continued in a similar or related business after prohibition. (R. 32.) The Board of Tax Appeals sustained the Commissioner and held that no deduction for obsolescence may be allowed where the assets were useful for other purposes and were used therefor after prohibition became effective. (R. 60.) The Circuit Court of Appeals, relying upon its decision in *Haberle Crystal Springs Brewing Co. v. Clarke*, 30 F. (2d) 219, held that, upon the conceded facts, the amounts claimed for obsolescence were justified and should have been allowed, and accordingly reversed the Board.

SPECIFICATION OF ERRORS TO BE URGED

The Circuit Court of Appeals erred—

I. In holding that where tangible assets of a taxpayer decline in value as a result of the extinguishment of its business by prohibition legislation the taxpayer may deduct from income any amount as obsolescence of such assets under Section 234 (a) (7) of the Revenue Act of 1918.

II. In holding that under the facts the taxpayer was entitled to deduct for the years 1918 and 1919 any amount for obsolescence of tangible property employed in its business.

REASONS FOR GRANTING THE WRIT

1. The decision in the present case is in conflict with and contrary to the decisions of this Court.

In *Clarke* v. *Haberle Brewing Co.*, 280 U. S. 384, this Court denied the taxpayer the right to deduct any amount from income under the provisions of Section 234 (a) (7) of the Revenue Act of 1918 for obsolescence of its good will during the time when it had become certain that such good will would be destroyed by prohibition legislation. This Court denied the deduction claimed on the ground that when a business is extinguished as noxious under the Constitution the owners can not demand compensation from the Government, or a partial compensation in the form of an abatement of taxes otherwise due, and that Congress could not have intended such partial compensation to be provided for by the words "exhaustion" or "obsolescence." This reasoning is equally applicable to a claim for deduction on account of obsolescence of tangible property of a brewing business proscribed by national prohibition.

In *Renziehausen* v. *Lucas*, 280 U. S. 387, the taxpayer claimed the right to deductions from income during the years 1918, 1919, and 1920 on account of obsolescence of good will and tangible property of a distilling business resulting from prohibition legislation. The claim was denied on the basis of the decision in the *Haberle Brewing Co. case*, and because of the additional fact that the taxpayer continued to manufacture whiskey for medicinal

purposes after national prohibition became effective and until the enactment of the Willis-Campbell Act of November 23, 1921, c. 134, 42 Stat. 222. In the instant case the taxpayer continued to use its plant and equipment in manufacturing near beer after national prohibition became effective.

2. The question is of present importance in administering the tax laws, since it is involved in cases now pending in the courts, the Board of Tax Appeals, and the Bureau of Internal Revenue. Without a decision of this Court, the Commissioner of Internal Revenue is unable to determine the proper principle to be applied in such cases, and an acceptance of the decision in this case would leave the matter in confusion. Although the Commissioner believes that the basis of this Court's decisions in the *Haberle Brewing Co.* and *Renziehausen cases* is equally applicable to the instant case, the confusion results from the fact that in the cited cases the discussion was confined to deductions for obsolescence of good will.

Wherefore, it is respectfully submitted that the petition should be granted.

WILLIAM D. MITCHELL,
Attorney General.

MARCH, 1930.

BRIEF IN SUPPORT OF PETITION

OPINION BELOW

The opinion of the Circuit Court of Appeals is not reported.

The findings of fact and opinion of the Board of Tax Appeals (R. 46–61) are reported in 13 B. T. A. 1040.

JURISDICTION

The order of the Circuit Court of Appeals reversing the decision of the Board of Tax Appeals was entered on December 16, 1929.

Jurisdiction is conferred upon this Court by Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTIONS PRESENTED

1. Where the imminence of prohibition legislation which will extinguish a taxpayer's business causes the tangible property employed in the business to decline in value, may the loss in value be deducted from income as obsolescence under Section 234 (a) (7) of the Revenue Act of 1918?

2. If deductions for obsolescence of tangible property resulting from prohibition legislation are allowable, is the taxpayer entitled to such deductions where it continued to use the property in the manufacture of near beer after national prohibition became effective?

STATUTE INVOLVED

The Revenue Act of 1918, c. 18, 40 Stat. 1057, 1077, 1078, provides in part:

SEC. 234(a) That in computing the net income of a corporation subject to the tax imposed by section 230 there shall be allowed as deductions:

* * * * *

(7) A reasonable allowance for the exhaustion, wear and tear of property used in the trade or business, including a reasonable allowance for obsolescence; * * *.

STATEMENT

A statement of the facts and of the errors relied upon will be found in the petition.

ARGUMENT

The Circuit Court of Appeals held that obsolescence occurs, resulting in a state more obsolete, when the property is less used or more neglected without forthwith rendering it entirely obsolete, and allowed as a deduction in computing net income the loss due to diminution in value of the property, resulting from the abolition of the business by prohibition legislation, during the period between the date such legislation became certain and the date when it went into effect. The Circuit Court of Appeals, as authority for this holding, relied upon its decision in *Haberle Crystal Springs Brewing Co.* v. *Clarke,* 30 F. (2d) 219, wherein it said (p. 220):

> A brewery may fairly be regarded as obsolete after prohibition, and as subject to obsolescence during the period between the date when such legislation became certain and the date when it went into effect.

Since the decision in the instant case this Court has reviewed on certiorari and reversed the decision of the Circuit Court of Appeals in the *Haberle Brewing Co. case* (*Clarke* v. *Haberle Brewing Co.*, 280 U. S. 384). In holding that the taxpayer was not entitled to deduct any amount from income under the provisions of Section 234 (a) (7) of the Revenue Act of 1918 for obsolescence of its good will by reason of impending prohibition legislation, this Court said (pp. 386–387):

> In our opinion the words now used can not be extended to cover the loss in this case and it is needless to speculate as to what other cases it might include. It seems to us plain without help from *Mugler* v. *Kansas*, 123 U. S. 623, that when a business is extinguished as noxious under the Constitution the owners can not demand compensation from the Government, or a partial compensation in the form of an abatement of taxes otherwise due. It seems to us no less plain that Congress can not be taken to have intended such a partial compensation to be provided for by the words "exhaustion" or "obsolescence." Neither word is apt to describe termination by law as an evil of a business otherwise flourishing, and neither becomes more applicable because the death is lingering rather than instantaneous. It is incredible that Congress by an Act approved on February 24, 1919, should have meant to enable parties to cut down their taxes on such grounds because of an amend-

ment to the Constitution that it had submitted to the legislatures of the States in 1917 and that had been ratified by the legislatures of a sufficient number of States the month before the present Act was passed.

Although the Court there dealt specifically with intangible property, the principle upon which the decision is based, namely, that Congress did not intend to allow an abatement of taxes through obsolescence deductions where the business had been extinguished by statute as noxious under the Constitution, would seem to be equally applicable to tangible property. It is submitted that the opinion of this Court in the *Haberle Brewing Co. case* is controlling herein and that no deductions from gross income representing losses or obsolescence of tangible or intangible property arising from or consequentially following upon the enactment of national prohibition are allowable.

Even if such deductions are proper with respect to tangible property, the taxpayer in the instant case did not establish its right to deductions before the Board of Tax Appeals. "Obsolescence" is the state of becoming obsolete and refers to a situation where the commercial usefulness of an asset will terminate before the end of its physical life. From its very nature, therefore, obsolescence begins only when from the existing facts the taxpayer has substantial reason to believe that the usefulness of the assets in his own or in any other business will end at some fairly definite time in the future when they

must be abandoned before the expiration of their normal physical life. This was not the situation of the taxpayer and the evidence supports the view that its tangible assets were not in a process of obsolescence during the years 1918 and 1919. The record shows that in 1917 the taxpayer began the manufacture of near beer, using the same machinery and equipment as that which it had used in manufacturing alcoholic beer. (R. 54, 58.) The machinery and equipment was continued in use for this purpose after prohibition legislation became effective. Its commercial usefulnes was not destroyed by such legislation and there was no basis for an obsolescence deduction.

In *Renziehausen* v. *Lucas,* 280 U. S. 387, the taxpayer claimed the right to deductions from income during the years 1918, 1919, and 1920 on account of obsolescence of good will and tangible property of a distilling business, resulting from prohibition legislation. The claim was denied on the basis of the decision in the *Haberle Brewing Co. case,* and because of the additional fact that the taxpayer continued to manufacture whiskey for medicinal purposes after national prohibition became effective and until the enactment of the Willis-Campbell Act on November 23, 1921, c. 134, 42 Stat. 222. The situation of the taxpayer in the instant case was similar to that of the taxpayer in the *Renziehausen case.*

It is submitted that the decision of the Circuit Court of Appeals is in conflict with the principles

upon which the above decisions of this Court were based, but that in view of the fact that the discussions in those decisions were confined to intangible assets the proper course to be followed by the Commissioner in disposing of pending cases involving tangible assets is left in doubt unless this Court will review the decision of the Circuit Court of Appeals.

CONCLUSION

In order that there may be a conclusive determination of this question involving a principle of statutory construction of present importance in administering the income tax laws, it is urged that this Court grant the petition.

Respectfully submitted.

WILLIAM D. MITCHELL,
Attorney General.

G. A. YOUNGQUIST,
Assistant Attorney General.

SEWALL KEY,

NORMAN D. KELLER,
Special Assistants to the Attorney General.

C. M. CHAREST,
General Counsel,
Bureau of Internal Revenue.

JOHN MACC. HUDSON,
Special Attorney,
Bureau of Internal Revenue.

MARCH, 1930.

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No. 61

In the Supreme Court of the United States

OCTOBER TERM, 1930

DAVID BURNET, COMMISSIONER OF INTERNAL REVENUE, PETITIONER

v.

NIAGARA FALLS BREWING COMPANY AND PAUL A. SCHOELLKOPF, CHARLES E. HAEBERLE, ET AL., ETC.

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF FOR THE PETITIONER

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NIAGARA FALLS BREWING COMPANY AND PAUL A. SCHOELLKOPF, CHARLES E. HAEBERLE ET AL., ETC.

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF FOR THE PETITIONER

OPINIONS BELOW

The findings of fact and opinion of the Board of Tax Appeals (R. 25–35) are reported in 13 B. T. A. 1040. The opinion of the Circuit Court of Appeals (R. 46–50) is reported in 38 F. (2d) 217.

JURISDICTION

The judgment of the Circuit Court of Appeals reversing the decision of the Board of Tax Appeals was entered on December 16, 1929. (R. 51.) The

petition for a writ of certiorari was filed March 15, 1930 (R. 51), and was granted by this Court on April 28, 1930 (281 U. S. 712).

The jurisdiction of this Court rests on Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTIONS PRESENTED

1. Did Congress intend by Section 234 (a) (7) of the Revenue Act of 1918 to authorize a deduction for obsolescence of tangible property in 1918 and 1919 caused by the imminence of prohibition legislation?

2. An alternative question is whether prohibition legislation caused a loss in regard to such tangible property in 1918 and 1919 which may be deducted under Section 234 (a) (4) of the Revenue Act of 1918.

3. The property which is the subject of the claimed deduction was used for the manufacture both of beer and near beer. Since prohibition legislation placed no restriction upon the continued use of the property for the manufacture of near beer, the question arises whether the deduction may in any event be allowed under the facts of this case.

STATUTE INVOLVED

The Revenue Act of 1918, c. 18, 40 Stat. 1057, 1077, 1078, provides in part:

> SEC. 234. (a) That in computing the net income of a corporation subject to the tax

imposed by section 230 there shall be allowed as deductions:

* * * * *

(4) Losses sustained during the taxable year and not compensated for by insurance or otherwise;

* * * * *

(7) A reasonable allowance for the exhaustion, wear and tear of property used in the trade or business, including a reasonable allowance for obsolescence;

* * * * *

STATEMENT

This case reached the Circuit Court of Appeals on the petition of respondents for a review of the decision of the Board of Tax Appeals determining deficiencies in income and profits taxes for the years 1918 and 1919 in the respective amounts of $18,561.17 and $5,013.65. (R. 40.) The case involves the tax liability of the respondent Niagara Falls Brewing Company, which was a New York corporation. It was voluntarily dissolved on December 1, 1921, and its affairs in dissolution are being administered by its directors as trustees in dissolution. They are also parties respondent in the present proceeding. (R. 32.)

The evidence is not reported in the record. The following is an epitome of the findings of the Board, supplemented by certain facts which are stated in its opinion (R. 26–35):

Prior to national prohibition the taxpayer was engaged in manufacturing and selling beer. Its business and good will were created by such manufacture and sale. At the time of its organization in 1902 it acquired the buildings and equipment of a joint-stock association, the name of which it took. Later it constructed new buildings and installed additional machinery and equipment, which were constructed and designed for the manufacture of beer and were not available for or readily adaptable to other uses. (R. 26.) In 1917 the taxpayer began the manufacture and sale of a beer of alcoholic content of less than one-half of one per centum, known as "Pep" or "near beer" or "cereal beverage." (R. 31, 33.) In its manufacture the taxpayer used the same machinery and the same process which it had used in making alcoholic beer, except that in making near beer the additional process of "dealcoholizing" was necessary. The near beer had the same appearance as the alcoholic beer manufactured by the taxpayer, but did not resemble it in taste, nor did it have the same popularity. (R. 33.) In 1918 the taxpayer also began the manufacture of other soft drinks. This required machinery different from that used for the manufacture of beer and near beer, and no part of the allowances claimed by the taxpayer relate to property used for the manufacture of these other soft drinks. (R. 31, 27.)

In October, 1919, the taxpayer discontinued the manufacture and sale of alcoholic beer because of

national prohibition, but it continued to make and sell near beer. (R. 31.)

The taxpayer, upon discontinuing the manufacture and sale of alcoholic beer, considered the possibility of adapting its plant to other manufacturing or commercial purposes, but the construction and condition of the buildings and machinery rendered them unsuitable and not adaptable for other uses, and removal of the machinery was not feasible. (R. 30.) When the sale of alcoholic beer was discontinued, the taxpayer abandoned the lower floor of one of its buildings, which had been devoted to storing and aging alcoholic beer, as its use was not required for near beer. (R. 31–32.) Thereafter one-half of another building, with the equipment therein, which had been used three or four times a week in manufacturing and bottling alcoholic beer, was used only about once every two weeks in making near beer. (R. 32.) Apparently the rest of the plant continued to be used regularly for making near beer. But sales of this beverage declined after the effective date of the Eighteenth Amendment (January 16, 1920), although the taxpayer did not lessen its efforts to make sales of this product. (R. 31.) In December, 1921, the respondent corporation was voluntarily dissolved, as it could not operate its business at a profit. (R. 32.) In January, 1922, it leased all of its buildings, plant and equipment under a lease originally running for three months, which

was renewable at the option of the lessee and which had been renewed continually up to the time of the hearing before the Board in 1927. (R. 32, 1.) The plant was used by the lessee for making near beer. (R. 34.)

There is no finding that it became apparent to the taxpayer in 1918 or 1919 that its property could not be used indefinitely in the near-beer business after prohibition should become effective.

The following facts do not appear in the record, but the Court may take judicial notice of them: The National Prohibition Amendment was adopted by both Houses of Congress in December, 1917. In the first six months of 1918 twelve States ratified the Amendment. Three more States ratified it during the remaining six months of 1918. In the early part of January, 1919, twenty-one more States ratified the Amendment, and on January 16, 1919, it became part of the Constitution, although it did not become effective until a year later.

The taxpayer charged against its earnings and deducted in its income-tax returns the sum of $110,047.52 in 1918 and the sum of $57,139.99 in 1919 for obsolescence of its buildings, machinery, and equipment used in the manufacture and sale of beer. (R. 29.) These deductions represented the figure which the taxpayer's officials considered necessary to bring the assets down to an amount realizable upon a forced or liquidation sale after prohibition should become effective. (R. 29.) The value of all the property used in the manu-

facture and sale of beer at the end of 1918 and 1919 was less than its depreciated cost or book value after deducting the amounts charged off for obsolescence of such property during those years. The difference between the value in 1918 and 1919 and the depreciated cost of taxpayer's property on December 31, 1917, was due to the imminence and incidence of war-time and permanent prohibition legislation. (R. 33.) As the amounts involved on the different items need not be considered here, we do not refer to them, but they appear in detail in the findings.

The Commissioner of Internal Revenue disallowed the deductions claimed, on the ground that the taxpayer continued in a similar or related business after prohibition. (R. 18, 20.) The Board of Tax Appeals sustained the Commissioner's disallowance on this ground. (R. 34–35.) The Circuit Court of Appeals held that, upon the conceded facts, the amounts claimed for obsolescence were justified and should have been allowed, and accordingly reversed the determination of the Board. (R. 50.)

SPECIFICATION OF ERRORS TO BE URGED

The Circuit Court of Appeals erred:

I. In holding that where tangible assets of a taxpayer decline in value as a result of prohibition legislation the taxpayer may deduct from income any amount as obsolescence of such assets under Section 234 (a) (7) of the Revenue Act of 1918.

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II. In holding that under the facts the taxpayer was entitled to deduct for the years 1918 and 1919 any amount for obsolescence of tangible property employed in the business.

SUMMARY OF ARGUMENT

The Revenue Act of 1918 does not authorize a deduction, either as obsolescence or as a loss, for the decline in value of property, whether tangible or intangible, resulting from the imminence and incidence of national prohibition legislation. The principle enunciated in *Clarke* v. *Haberle Brewing Co.*, 280 U. S. 384, is applicable here.

In any event there was no obsolescence in fact. To sustain a claim for deduction for obsolescence, it must appear that the taxpayer foresaw with reasonable certainty that the property would not be useful in his business or any other business, at some definite time in the future, when such property would have to be abandoned. There is no finding that this occurred during 1918 or 1919, the taxable years in question. Obsolescence results from a lack of usefulness and not from a lack of use. Here the taxpayer commenced to manufacture near beer in 1917, using the same property and equipment as was used to manufacture beer. The imminence of prohibition legislation did not justify the conclusion that it would affect the manufacture and sale of near beer or shorten the useful life of the property. After the adoption of national prohibition the taxpayer continued the manufacture

and sale of near beer. Its failure to use the property to as great an extent as before was due not to any lack of usefulness but solely to an absence of a large demand for the product.

There was no sale or abandonment of the property until 1928, and consequently there is no basis for the respondents' alternative contention that they are entitled to the deductions claimed in 1918 and 1919 as a business loss in those years.

ARGUMENT

I

CONGRESS DID NOT INTEND TO AUTHORIZE A DEDUCTION FOR OBSOLESCENCE OR LOSS OF TANGIBLE PROPERTY CAUSED BY PROHIBITION LEGISLATION

This Court has already decided that Congress did not intend by Section 234 (a) (7) of the Revenue Act of 1918 to authorize a deduction for obsolescence caused by prohibition legislation. *Clarke* v. *Haberle Brewing Co.*, 280 U. S. 384. The decision in that case was announced January 27, 1930, after the court below had decided the instant case. (R. 46.) Although the *Haberle* case involved the application of the obsolescence provision to good will, we submit that the reasoning is equally applicable to tangible assets. The Circuit Court of Appeals for the Second Circuit in its latest decision on the subject has so held. *V. Loewers Gambrinus Brewery Co.* v. *Anderson*, 42 F. (2d) 216, now pending in this Court upon a writ of certiorari granted October 20, 1930, No. 352, October Term, 1930.

In the *Haberle Brewing Co.* case, this Court said (pp. 386–387):

> In our opinion the words now used can not be extended to cover the loss in this case and it is needless to speculate as to what other cases it might include. It seems to us plain without help from *Mugler* v. *Kansas,* 123 U. S. 623, that when a business is extinguished as noxious under the Constitution the owners can not demand compensation from the Government or a partial compensation in the form of an abatement of taxes otherwise due. It seems to us no less plain that Congress can not be taken to have intended such a partial compensation to be provided for by the words "exhaustion" or "obsolescence." Neither word is apt to describe termination by law as an evil of a business otherwise flourishing, and neither becomes more applicable because the death is lingering rather than instantaneous. It is incredible that Congress by an Act approved on February 24, 1919, should have meant to enable parties to cut down their taxes on such grounds because of an amendment to the Constitution that it had submitted to the legislatures of the States in 1917 and that had been ratified by the legislatures of a sufficient number of States the month before the present Act was passed.

Renziehausen v. *Lucas,* 280 U. S. 387, presented the same question as the *Haberle* case and was decided upon the authority of that case. The right

to a deduction for obsolescence of certain tangible property, as well as for obsolescence of good will, was involved in the *Renziehausen* case. The following facts appear in the record in that case, although they are not stated in the opinion of this Court: In his appeal from the Commissioner's determination, Renziehausen claimed the right to a deducion for obsolescence of good will and also of his plant, equipment, and warehouses for the years 1918 to 1921, inclusive. The Board of Tax Appeals allowed a deduction in 1921 on account of the obsoleteness of plant and equipment (not including warehouses), caused by the enactment of the Willis-Campbell Act on November 23, 1921, and further held that obsolescence of the warehouses began in 1921 and that the taxpayer was entitled to such deductions in 1921 and 1922. The Board disallowed deductions for obsolescence of good will and of the tangible property in 1918, 1919, and 1920. On appeals by both parties, the Circuit Court of Appeals for the Third Circuit affirmed the decree of the Board. The taxpayer alone applied for a writ of certiorari. In this Court the Government opposed the allowance claimed for obsolescence of the tangible property in 1918, 1919, and 1920 (and claimed in the alternative as a business loss) on the ground that the enactment of the Willis-Campbell Act in 1921 was unforeseen and therefore that obsolescence had not commenced in 1918, 1919, and 1920. The Government also opposed any allowance for obsolescence of good will. This Court said (p. 389):

> * * * What has been said in the *Haberle Crystal Springs Brewing Co.'s* case is sufficient to dispose of this one, and here there is the additional fact that in 1919 the petitioner became aware that he could manufacture whiskey for medicinal purposes and did so until the Willis-Campbell Act of November 23, 1921, c. 134; 42 Stat. 222, was passed and the petitioner failed to obtain a permit under it. The evidence does not seem to warrant an alternative claim under the Revenue Act of 1918, § 214 (a) (4), for losses incurred in business in 1919, even if otherwise it could be sustained.
>
> * * * The petitioner has no reason to complain of the allowance for obsolescence of the warehouses.

In view of the contentions of the Government in that case, we are not certain that this Court intended to deny the deduction for obsolescence of the tangible property upon the same ground upon which it denied the deduction on account of good will. But regardless of what was decided there, we conclude that the broad ground of decision of the *Haberle Brewing Co.* case is applicable to the deduction claimed here.[1] And it seems obvious that

---

[1] There are several early rulings of the Bureau of Internal Revenue holding that deductions were proper for obsolescence resulting from prohibition legislation. See 1 Cumulative Bulletin, April–December, 1919, pp. 125, 127, 133; 2 Cumulative Bulletin, January–June, 1920, p. 143; 5 Cumulative Bulletin, July–December, 1921, p. 142; III–1 Cumulative Bulletin, January–June, 1924, p. 148.

Congress had no different intent with respect to losses under Section 234 (a) (4) than it had with respect to obsolescence under Section 234 (a) (7) (pp. 2–3, *supra*).

II

EVEN IF THE STATUTE SHOULD BE CONSTRUED TO PROVIDE FOR DEDUCTIONS FOR OBSOLESCENCE OR LOSS OF BREWERY PROPERTY CAUSED BY PROHIBITION, THERE IS NO GROUND FOR SUCH A DEDUCTION HERE, AS THE PROPERTY FOR WHICH THE DEDUCTION IS CLAIMED WAS ALSO USED IN THE MANUFACTURE OF NONINTOXICATING BEER

We contend that there was no obsolescence in fact during 1918 or 1919.

Obsolescence is the state of becoming obsolete. Property is obsolete when it is no longer useful for the purpose for which it was acquired and can not be used for any other purpose. From its very nature, obsolescence begins only when there is a reasonable certainty that the property will become obsolete. As the Circuit Court of Appeals for the Ninth Circuit said of obsolescence in *Lassen Lumber & Box Co.* v. *Blair*, 27 F. (2d) 17, 18–20:

> * * * in no case can a deduction be demanded for an anticipated depreciation of that character until there is a reasonable certainty that it will take place. * * *
>
> * * * * *
>
> * * * the taxpayer can not require proof that the requisite contingencies will not happen; but the burden is upon it to

> establish with a reasonable degree of certainty that they will occur * * *.
>
> * * * Depreciation from day to day and year to year, resulting from wear and tear or other physical deterioration, is susceptible to present estimate. But in a sense the depreciation here claimed does not accrue until the end of the period of use; presently it is constructive only. While upon the assumption that the loss will, in fact, be incurred, it is but fair to spread it ratably over the entire period, it is also only fair to require that it be shown by a preponderance of proof that its occurrence in the future is reasonably or practically certain to take place. A possibility or mere probability is not enough. * * *

Whether property is becoming obsolete is a question of fact. The burden was upon taxpayer to show that it was entitled to the deduction which the Commissioner had disallowed and that the additional tax was to that extent illegally assessed. *Botany Mills* v. *United States*, 278 U. S. 282, 289–290; *Reinecke* v. *Spalding*, 280 U. S. 227, 232–233; *Niles Bement Pond Co.* v. *United States*, 281 U. S. 357, 361.

There is no finding that at any time during the taxable years in question it became apparent that the property would become obsolete, and we submit that no inference to this effect can properly be drawn from any of the facts which are recited.

We do not deny that it was apparent as early as 1918 that prohibition was imminent, but this would not prevent the taxpayer from manufacturing near beer, and there is little in the record to indicate what the prospects for success in this business were in 1918 and 1919. The taxpayer evidently began the manufacture of near beer or cereal beverage in 1917. A tabulation of sales of its products shows that the "sales" of this beverage (probably meaning deliveries) were very small until 1920, when they became substantial, and that they fell off materially in 1921. (R. 30.) The findings also state that after the Eighteenth Amendment became effective (January 16, 1920) the taxpayer's "sales" (probably meaning new contracts for sale) of near beer declined. (R. 31.) It was evidently not until some time in 1921 that the taxpayer came to the conclusion that it could not operate its business at a profit. (R. 32.) Although it seems fair to call attention to the statement in the findings that assets of a similarly situated brewing company at Niagara Falls were sold for a very low sum in 1919, and apparently the market was flooded with brewing machinery then (R. 28), these considerations do not seem to us sufficient to establish the position which the respondents must take.

The business of manufacturing near beer was in all essential respects of the same character as that of making alcoholic beer, except that the man-

ufacture of near beer required the additional process of "dealcoholization." The same buildings, machinery, and equipment were used by the taxpayer and, after its dissolution, by its lessee in making near beer which had been used in making beer. It is true that one floor of one building was not used after the cessation of beer brewing and that a part of another building was used much less frequently after prohibition. But it does not appear that these buildings were not useful for manufacturing near beer. Their disuse resulted from the lack of necessity for full use of the plant. They were not obsolescent, but were idle simply because of decreased volume of business. We submit that obsolescence can not be predicated upon a mere lessening of use. The failure to use machinery or a building to its full capacity should not support a deduction for obsolescence.

The court below did not discuss the point now under consideration; nor did it advert to the statement in the opinion of the Board (R. 34):

> * * * If we were disposed to hold that obsolescence were allowable on account of abandonment of a part of a building, we do not have sufficient evidence to determine whether the amount contended for by the petitioner is correct or what the allowance should be. The contention therefore must be denied.

In *Renziehausen* v. *Lucas, supra*, the claim for obsolescence was denied on the reasoning of the

Haberle Brewing Co. case and because of the additional fact that the taxpayer continued to manufacture whiskey for medicinal purposes after national prohibition became effective until the enactment of the Willis-Campbell Act on November 23, 1921 (c. 134, 42 Stat. 222). The situation of the taxpayer in the instant case was similar in that respect to that of the taxpayer in the *Renziehausen* case.

The evidence does not warrant the alternative claim under Section 234 (a) (4) of the Revenue Act of 1918 (*supra*, p. 3) for losses incurred in business in 1918 and 1919. This provision necessarily requires that there be a complete and definitely ascertained loss, fixed by an identified event such as an actual abandonment, sale, or destruction of the property. *United States* v. *White Dental Co.*, 274 U. S. 398, 401; Cf. *Lewellyn* v. *Elec. Reduction Co.*, 275 U. S. 243, 246–247; *Lucas* v. *American Code Co.*, 280 U. S. 445, 449.

Ordinarily, there must be a sale or other final disposition of the property before it can be said that a deductible loss has been sustained. In exceptional cases where the usefulness of business assets is suddenly terminated and the business is discontinued, or the property is discarded or permanently abandoned, a deductible loss may result. But in the latter event there must be a complete and final abandonment of the property for which the

loss is claimed.[2] It was not until October 29, 1919, that the manufacture and sale of real beer ceased. (R. 30–31.) It is clear, therefore, that there could have been no loss in 1918. And we contend that, as the taxpayer continued to use, own, or lease the plant until it sold the property in 1928 (R. 32, 36), it could not take a loss on account of diminution of its value until that year, if ever.

Under these circumstances, it can not be said that respondent sustained a deductible loss in 1919. Cf. *Dick & Bros. Brewing Co.* v. *United States,* 67 C. Cls. 505. The most that can be said is that this property suffered a substantial decline in value, but "The statute obviously does not contemplate and the regulations * * * forbid the deduction of losses resulting from the mere fluctuation in value of property owned by the taxpayer." *United States* v. *White Dental Co., supra,* p. 401.

We therefore maintain that the taxpayer was not entitled to deductions in 1918 and 1919 for the decline in value of its buildings, machinery, and equipment, either as obsolescence or as losses sustained in such years.

---

[2] The regulations promulgated by the Treasury Department (*infra*, p. 20), under paragraphs 4, 5, and 6 of Section 214(a) of the 1918 Act, relating to the deduction of losses, provided that a deduction on account of buildings could be made only when they were sold or "permanently abandoned or permanently devoted to a radically different use," and as to machinery only when sold or "when its use as such is permanently abandoned."

CONCLUSION

The decree of the Circuit Court of Appeals should be reversed and the order of the Board of Tax Appeals should be affirmed.

Respectfully submitted.

THOMAS D. THACHER,
Solicitor General.
G. A. YOUNGQUIST,
Assistant Attorney General.
CLAUDE R. BRANCH,
SEWALL KEY,
J. LOUIS MONARCH,
JOHN MACC. HUDSON,
Special Assistants to the Attorney General.
C. M. CHAREST,
General Counsel,
Bureau of Internal Revenue.

DECEMBER, 1930.

APPENDIX

Treasury Regulations 45, promulgated April 17, 1919, under the Revenue Act of 1918, contains the following:

> ART. 143. *Loss of useful value.*—When through some change in business conditions the usefulness in the business of some or all of the capital assets is suddenly terminated, so that the taxpayer discontinues the business or discards such assets permanently from use in the business, he may claim as a loss for the year in which he takes such action the difference between the cost or the fair market value as of March 1, 1913, of any asset so discarded (less any depreciation allowances) and its salvage value remaining. This exception to the rule requiring a sale or other disposition of property in order to establish a loss requires proof of some unforeseen cause by reason of which the property must be prematurely discarded, as, for example, where machinery or other property must be replaced by a new invention, or where an increase in the cost of or other change in the manufacture of any product makes it necessary to abandon such manufacture, to which special machinery is exclusively devoted, or where new legislation directly or indirectly makes the continued profitable use of the property impossible. This exception does not extend to a case where the useful life of property terminates solely as a result of those gradual processes for which depreciation allowances are authorized. It does not apply to inventories

or to other than capital assets. The exception applies to buildings only when they are permanently abandoned or permanently devoted to a radically different use, and to machinery only when its use as such is permanently abandoned. Any loss to be deductible under this exception must be charged off on the books and fully explained in returns of income. But see articles 181–188.

U. S. GOVERNMENT PRINTING OFFICE: 1939

FILE COPY

No. 61

APR 12 1930
CHARLES ELMORE CROPLEY

IN THE

Supreme Court of the United States

October Term, 1929.

ROBERT H. LUCAS, Commissioner of Internal Revenue,
Petitioner,

vs.

NIAGARA FALLS BREWING COMPANY, and PAUL A. SCHOELLKOPF, CHAS. E. HAEBERLE, FRED H. KRULL, EDSON P. PFOHL, ALBERT T. MAYLE, FREDERICK CHORMANN, RUDOLF V. ROSE, and GEORGE F. NYE, as Directors of said Company and Trustees Thereof in Dissolution,
Respondents.

RESPONDENTS' BRIEF OPPOSING CERTIORARI

BATAVIA TIMES, LAW PRINTERS,
BATAVIA, N. Y.

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1929.

No. 741.

ROBERT H. LUCAS, Commissioner of Internal Revenue,
Petitioner,

v.

NIAGARA FALLS BREWING COMPANY, *et al.*,
Respondents.

RESPONDENTS' BRIEF OPPOSING CERTIORARI

Opinion Below.

The opinion of the Circuit Court of Appeals (R. 46-50) is not reported.

The opinion and findings of fact of the Board of Tax Appeals are reported in 13 B. T. A., 1040.

Jurisdiction.

The jurisdiction of this Court depends upon Section 240 (a) of the Judicial Code as amended by the act of February 13, 1925, and Section 1003 of the Revenue Act of 1926 (Act of February 26, 1926). The Circuit Court of Appeals for the Second Circuit reversed the decision of the

Board of Tax Appeals by an order entered in the office of the Circuit Court of Appeals December 16, 1929.

Questions Presented.

(1) Whether the Commissioner of Internal Revenue can, by regulation, increase the burden of the tax statute [Revenue Act of 1918, C. 18, 40 Stat., 1057, 1077, 1078, 234a (7) quoted in petitioner's brief (Page 9)] by requiring as a condition for the allowance of deductions for obsolescence that the taxpayer shall abandon the assets upon which the obsolescence deduction is claimed.

(2) Whether the taxpayer by continuing to make a cereal beverage which did not resemble taxpayer's former product either in taste or popularity, but did resemble it in appearance and was partly produced by the same machinery (R. 33) thereby failed to conform to the regulation requiring abandonment of the assets.

(3) Whether the abandonment of part of two buildings and the greatly reduced use of certain machinery was a partial abandonment of each sufficient to sustain obsolescence deductions thereon under the regulation.

These questions are referred to on Page 8 of the petitioner's brief under "Questions Presented," Paragraph 2.

The question, now contained in Paragraph 1 on Page 8 of petitioner's brief and as Specification No. 1 of "Errors to be Urged" in the petition at Page 5, whether claims for obsolescence of tangible property can be based on the imminence of prohibition legislation was neither raised, argued nor considered, before or by the Circuit Court of Appeals.

"The taxing authorities do not deny that legislation which shortens the useful life of tangible assets entitles the taxpayer to an allowance for obsolescence under the 1918 act. (Appeal of Manhattan Brewing Co., 6 B. T. A. 952, which allowed obsolescence of tangibles but not of good will, because of the imminence of prohibition.)" (R. 50.)

This is further evidenced by the Summary of Argument of the Commissioner in his brief there, set forth as Appendix "A," annexed hereto.

"As the above rulings * * * were not assigned as errors in the Circuit Court of Appeals and were not considered by it, they cannot be insisted upon here as grounds for reversal."

(*Ana Maria Sugar Company vs. Quinones*, 254 U. S. 245, 251; 65 L. Ed. 246, 249.)

Statement.

The following statement is deemed necessary to correct inaccurate statements in the petition (Page 2). The Board of Tax Appeals found that the petitioner continued to make "near beer" in order to see if the plant could be made to pay by making this product, also to keep the plant in action and save the machinery. The decision of the Circuit Court of Appeals did not merely follow its decision in *Haberle Crystal Springs Brewing Company vs. Clarke*, as implied at Page 5 of the petition for certiorari. The opinion of the Court (R. 46-50) clearly indicates that the Court was concerned with the lawfulness of the Commissioner's requirement that the assets be abandoned before they could be considered obsolescent (R. 41, 50), and decided that question for taxpayer under previous decisions of this Court.

Argument.

The decision of the Circuit Court of Appeals conformed to the decisions of the Board of Tax Appeals in other cases where obsolescence deductions had been granted although the assets upon which the deductions were based were not abandoned.

Manhattan Brewing Company, 6 BTA, 952.
Maltibestos Company, 6 BTA, 1060.
Corsicana Gas & Electric Company, 6 BTA, 565.
J. Chr. G. Hupfel, Inc., 9 BTA, 944.
Seas Shipping Company, Inc., v. Commissioner, 16 BTA, 841.

It was also in accordance with the decision of the Circuit Court of Appeals for the District of Columbia in *National Industrial Alcohol Company vs. Commissioner*, decided February 4, 1930, U. S. Daily, February 12, 1930, Vol. IV, No. 291, p. 4, not otherwise reported. No conflicting decision has been made by any Circuit Court of Appeals or the Court of Appeals for the District of Columbia.

The opinions in *Haberle Crystal Springs Brewing Company vs. Clarke*, and *Renziehausen vs. Commissioner*, in this Court, held only that brewery and distillery good will and other intangible assets could not properly be the subject of a deduction in computing income tax on account of their obsolescence due to prohibition. These intangibles are not distinguishable from "the business of brewing and distilling," which was discontinued by prohibition.

As indicated in the cases previously cited, it has been the well settled law for many years that the tangible assets used in brewing are as much a subject of a deduction in computing income tax, on account of their loss of usefulness, as the tangible assets of any other business, whether such loss of usefulness or obsolescence be due to the prog-

ress of the art or the cessation of the art through government interposition. That the Commissioner through regulation could not lay an extra burden upon the taxpayer by way of requiring entire immediate abandonment of the assets has also been the settled law for many years under the decisions of this Court, upon which the decision of the Circuit Court of Appeals was based (R. 50).

International R. R. Co. v. Davidson, 257 U. S. 506, 42 S. Ct. 179, 66 L. Ed. 341.

United States v. George, 228 U. S. 14, 33 S. Ct. 412, 57 L. Ed. 712.

Williamson v. United States, 207 U. S. 425, 28 S. Ct. 163, 52 L. Ed. 278.

The distribution of the funds of respondent Brewing Company to its stockholders has been suspended for many years by the pendency of this assessment, which is contrary to law. During the suspension the funds are unproductive. The decision of the Circuit Court of Appeals herein has served the ends of justice by permitting this taxpayer, as others similarly situated have been permitted, to deduct from its income derived from the final sales of its product in 1918 and 1919 the undisputed losses due to the obsolescence of its machinery and other tangible assets from government intervention. That decision should not be disturbed nor should its effect in releasing the funds of the taxpayer for distribution to its stockholders be delayed by the issuance of a certiorari writ. Nor should the taxpayer be put to further expense in resisting this unlawful additional assessment. For these reasons the respondent opposes the issuance of the writ.

Respectfully submitted,

BASIL ROBILLARD,
Counsel for Respondents.

APPENDIX "A".

Quotation from petitioner's brief before the Circuit Court of Appeals demonstrating that its assignment of Specification of Errors to be Urged No. 1 set forth in the petition at Page 5 was not argued or considered below:

"SUMMARY OF ARGUMENT.

"The petitioner is not entitled to deductions in the taxable years for the decline in value of its buildings, machinery, and equipment either as obsolescence or as losses sustained in such years.

"Obsolescence is the process of becoming obsolete and is an allowable deduction in a case where it is reasonably apparent that the commercial usefulness of an asset will end before the expiration of its physical usefulness. At the time that national prohibition became imminent the petitioner corporation began the manufacture of near beer in addition to its manufacture of beer of alcoholic content, using the same buildings, machinery, and equipment. It continued to manufacture near beer until its dissolution in 1921, and its plant was thereafter used for the same purpose by a lessee. As there was no lack of usefulness but only a reduced employment of the petitioner's plant due to the smaller demand for near beer, and since it could not be reasonably apparent during the taxable years that the commercial usefulness of the property would terminate before the end of its physical usefulness, a deduction for obsolescence was properly denied.

"The petitioner did not suffer a deductible loss, since there was no sale, abandonment, or other disposition of its property during the taxable year within the meaning of the Regulations and the intendment of the Act, and deductions for losses are not proper when there is only a fluctuation in the value of property. *United States v. White Dental Co.*, 274 U. S. 398, 401."

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IN THE

Supreme Court of the United States

October Term, 1930.

DAVID BURNET, Commissioner of Internal Revenue,
Petitioner,

vs.

NIAGARA FALLS BREWING COMPANY, *et al.*,
Respondents.

No. 61.

RESPONDENTS' BRIEF.

BASIL ROBILLARD,
Counsel for Respondents,
425-443 Gluck Building,
Niagara Falls, N. Y.

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BATAVIA, N. Y.

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IN THE

Supreme Court of the United States

OCTOBER TERM 1930.

DAVID BURNET, Commissioner of Internal Revenue, *Petitioner,* vs. NIAGARA FALLS BREWING COMPANY, *et al.,* *Respondents.*	No. 61.

RESPONDENTS' BRIEF.

Opinions Below.

The Board of Tax Appeals (R. 25-35), 13 B. T. A., 1040.

Circuit Court of Appeals (R. 46-50), 38 F. (2nd) 217.

Necessary Additional Statement of Case.

The buildings and equipment of Taxpayer upon which the obsolescence deduction was taken, are not available or practicable for use in any business except the manufacture of spirituous and malt liquors, which has been prohibited. (R. 7 §9 [o]; R. 22 §§9, 13; R. 30.)

The depreciated cost of the land, buildings and equipment on December 31st, 1917, was (R. 27)		$477,054.60
This depreciated cost was the actual value of the assets on that date. (R. 28.)		
The Taxpayer took obsolescence deduction for 1918 thereon of	$110,047.52	
and for 1919 of	57,139.99	$167,187.51
The regular depreciation for the two years as approved by the Commissioner was	30,750.01	$197,937.52
The book value on December 31, 1919, after the depreciation and obsolescence had been taken was therefore		$279,117.08
The actual value of the assets during the years 1918 and 1919 (R. 32, 33) was		80,475.00
or		$198,642.08

less than the book value thereof after the deduction for obsolescence had been made. (R. 32, 33.) This reduction in value was due to prohibition legislation. (R. 33.) The city assessments of the property were substantially reduced solely on account of the effect of prohibition upon the property. (R. 31.)

Contrary to the Commissioner's contention at pages 6, 8 and 14 of his brief, there are findings (R. 28, 29) that the officers, directors and stockholders of the respondent

during 1917, 1918, and 1919 foresaw that the property would diminish in value by reason of imminent prohibition. The evidentiary facts upon which the findings were made were stipulated in the trial court. The Commissioner's counsel have changed, and the misapprehension of present counsel is obviously due to unfamiliarity with this stipulation, which is annexed to this brief as Appendix "A." The facts showing foreknowledge and anticipation of loss through prohibition appear at paragraphs 11-29 of it (pp. 21-30 *infra*). Moreover, it is found that the obsolescence deductions were based upon the sale by a similar company of its assets for less than book value after a much greater obsolescence deduction. (R. 29.)

The respondent abandoned the business of making beer in 1919. (R. 30.) The plant was located in an industrial zone under the city zoning law. (R. 30.) The buildings could not be used for any other purpose than the manufacture and sale of malt and spirituous liquors, which has been prohibited. (Petition, §9, par. [o], R. 7; Answer, §§9, 13, R. 22.) Extensive efforts to convert the premises and machinery for other manufacturing purposes were unavailing (R. 30), and the machinery could not be removed from the building without dismantling the machinery and tearing out a side of the building. (R. 30.)

Respondent's sales of beer diminished 15.8% from 1917 to 1918, and 40.9% from 1918 to 1919 (R. 30) due to war time prohibition, and from 1918 to 1919 its sales of cereal beverage decreased 97.5% (R. 30).

Respondent's best efforts to sell the premises resulted in no offer higher than $35,000 (R. 31). The highest rental

it could obtain for the entire plant was $5,000 a year, net (R. 32).

These findings conclusively show that the respondent must have known that its business and plant would become obsolete and of greatly reduced value when prohibition became completely effective January 1st, 1920, and as it became partly effective during the years 1918 and 1919.

Summary of Argument.

The tangible business property used in brewing, like any other business equipment, may be subject to obsolescence and the basis of an obsolescence deduction in computing taxable income, although intangibles such as good will may not. Wartime prohibition and national prohibition caused an obsolescence of this brewing equipment. The Commissioner exceeded his lawful powers when by regulation he attempted to condition the obsolescence deduction upon the immediate abandonment of the equipment. The taxpayer satisfied even this regulation when it abandoned the brewing of beer but continued to use the equipment to produce a drink resembling beer neither in effect, taste nor popular demand but in appearance only. The total abandonment of part of one building and the abandonment of 84% of the use of another were sufficient to satisfy any interpretation of the regulation as to these assets. There was an actual realized loss upon the equipment; the abandonment of the brewing business closed the transaction and the owner should not be compelled to pay income and profits tax upon that part of its income represented by this loss.

ARGUMENT

POINT I.

Brewery Tangibles may be the subject of deduction for obsolescence in computing income tax.

The statute is Section 234 (a) of the Income Tax Act of 1918:

> "Sec. 234. (a) That in computing the net income of a corporation subject to the tax imposed by section 230 there shall be allowed as deductions:
>
> * * * * * * *
>
> (4) Losses sustained during the taxable year and not compensated for by insurance or otherwise;
>
> * * * * * * *
>
> (7) A reasonable allowance for the exhaustion, wear and tear of property used in the trade or business, including a reasonable allowance for obsolescence;"

The Board of Tax Appeals found every necessary fact to establish the right to an obsolescence deduction upon these tangibles, viz., the obsolescence, the cause of obsolescence, the amount thereof (R. 33), the depreciated book cost of the assets on March 1st, 1913, and the value of them on that date (R. 31, 32), the depreciated cost of them at the commencement of the obsolescence period and their value on that date (R. 27, 28), the salvage value at the end of the obsolescence period (R. 33), and the fact that the taxpayer was aware of the obsolescence during the period and prior to it (R. 28).

The taxpayer did not seek any deduction on account of obsolescence of good will or any other inherent element of its business discontinued by prohibition. The deduction was limited to obsolescence or loss of the tangible equipment with which it did the work which was ended by prohibition (R. 33)—its buildings and machinery.

The decision in *Clarke vs. Haberle Crystal Springs Brewing Company*, 280 U. S., 384, does not apply to this case until expanded to hold that the tools of brewing are so attainted by their use that the loss to the owner from obsolescence of them is not cognizable under the tax law. The Eighteenth Amendment to the Constitution prohibits the business but contains no intimation that the tools of the business are forfeit. It was certain that the equipment would become obsolete when prohibition became effective January 16th, 1920.

Obsolescence of equipment is frequently due to the progress in an art. Here it is due to progress out of the art through national legislation. The statutory permission to deduct from income a reasonable allowance for the obsolescence of these tools should be vouchsafed to the brewer as to the miner, the tobacconist, or any other producer.

> "There is nothing to suggest that the word 'property' is used in any restricted sense." said this Court of the same phrase in the prior act.
>
> *Lynch vs. Alworth-Stephens Co.*, 267 U. S., 364, 369.

Examination of the congressional history of the Act shows no contrary intention but only that the obsolescence deduction should be of general application.[1]

---

1. 65th Congress, Bill H. R. 12863, House Report: H. Doc., Vol. 114, No. 1267, Serial 7444, in which the bill as reported to the House read, Sec. 234 (7): "A reasonable allowance for the exhaustion, wear and tear of property used in the trade or business, but in the case of a foreign corporation only as to property within the United States."

The Senate amendment, No. 147, Sen. Doc., 310, Vol. 4, Serial 7460, read: "A reasonable allowance for the depreciation of property used in the trade or business."

The Conference Committee in H. R. 1037, Vol. 1, Serial 7454, recommended: "That the House recede from its disagreement to the amendment of the Senate No. 147 and agree to the same with an amendment as follows: 'Omit the matter inserted by amendment and reinsert the matter stricken out by said amendment, and on Page 37, line 24 of the bill, after "business" insert a comma and the following "including a reasonable allowance for obsolescence"; and the Senate agree to the same.'"

Mr. Kitchen, Chairman of the Conference Committee, reported for it, C. R., Vol. 67, p. 2991, on Amendment No. 147:

"The House Bill provided that in determining net income a reasonable allowance shall be made for exhaustion, wear and tear of the property used in the trade or business. The Senate amendment provides that a reasonable allowance shall be made in computing net income for the depreciation of property used in the trade or business. The House receded with an amendment providing that in computing net income a reasonable allowance shall be made for the exhaustion, wear and tear of the property used in the trade or business, including a reasonable allowance for obsolescence."

An examination of the congressional history of the Eighteenth Amendment[2] reveals no congressional intention that brewers should be denied the tax privileges of other citizens.

The decision in *Renzichausen vs. Lucas*, 280 U. S., 387, does not determine the question. There the taxpayer was allowed obsolescence of tangible property by the Board of Tax Appeals. This was affirmed by the Circuit Court of Appeals and upon certiorari this Court, following the Haberle case refused to permit the deduction for the value of the good will element of the very business and also refused to increase the allowance for the obsolescence of the warehouse or to apportion the obsolescence of the plant to years when the obsolescence was not to be anticipated.

V. Loewers Gambrinus Brewery Co. v. Anderson, 42 F. (2nd), 216, is obviously a decision of attempted conformity without any consideration of the essential difference between the good will as part and parcel of the very business (*Red Wing Malting Co. vs. Willcutts*, 15 F. (2) 623, 626) and the tools used in the business. The writ of limited certiorari already granted indicates that the Court has this view of that decision (No. 352 October Term).

In *National Industrial Alcohol Company vs. Commissioner*, 38 F. (2d) 718 (decided Feb. 4, 1930) the Court of Appeals of the District of Columbia without reference to the case at bar reached the same conclusion for the allowance of deductions on obsolescent tangible assets sustained by the opinion in the Court below in this case (R. 46-50).

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2. House Joint Resolution 84, H. Rp. No. 1493, Ser. 7110; Senate Joint Resolution 17, S. Rp. Vol. 1, No. 52, Ser. 7249; H. Rp. Vol. 1, No. 211, Ser. 7307.

POINT II.

The statute requires no abandonment of assets as a condition to an obsolescence deduction and the regulations of the department introducing such a condition precedent are void.

The statute contains no definition of the word "obsolescence." Webster's Dictionary defines it as "the state of becoming obsolete" and "obsolete" as "no longer in use; disused; neglected." Obsolescence is therefore "the state of becoming no longer in use, the state of becoming disused, or the state of becoming neglected." The Standard Dictionary defines "obsolescence" as "the condition or process of gradually falling into disuse; no longer practiced or accepted, of a discarded type or fashion, bygone, antiquated." The taxpayer's equipment in 1918 and 1919 conformed to these definitions as the findings show (R. 32, 33).

No provision of the statute requires obsolescent assets to be abandoned. The Commissioner of Internal Revenue, however, promulgated the regulation known as Article 143 of Regulations 45, as follows:

> "Loss of Useful Value.—When through some change in business conditions the usefulness in the business of some or all of the capital assets is suddenly terminated so that the taxpayer discontinues the business or discards such assets permanently from use in the business, he may claim as a loss for the year in which he takes such action the difference between the cost or the fair market value as of March 1, 1913, of any asset so discarded (less any depreciation allowances) and its salvage value remaining. This exception to the rule requiring a sale or other disposition of property in order to establish a loss requires proof of some unforeseen cause by reason of which the property must be prematurely discarded as for example, where ma-

chinery or other property must be replaced by a new invention, or where an increase in the cost of or other change in the manufacture of any product makes it necessary to abandon such manufacture to which special machinery is exclusively devoted, or where new legislation directly or indirectly makes the continued profitable use of the property impossible. This exception does not extend to a case where the useful life of property terminates solely as a result of those gradual processes for which depreciation allowances are authorized. It does not apply to inventories or to other than capital assets. The exception applies to buildings only when they are permanently abandoned or permanently devoted to a radically different use, and to machinery only when its use as such is permanently abandoned. Any loss to be deductible under this exception must be charged off on the books and fully explained in returns of income. But see articles 181-188."

This regulation adds an additional burden to the tax statute, viz.: the condition that obsolescent property must be finally abandoned as obsolete and its use terminated before obsolescence deductions will be permitted for it. The regulation mistakes *obsoleteness* for obsolescence and ignores the obvious fact that obsol*escence* frequently occurs to make an asset more obsolete, less used and more neglected without forthwith rendering it entirely obsolete, useless and fit only to be abandoned.

The right to take a reasonable deduction for obsolescence was given by the Act of February 24, 1919, Section 234 (a) (7) quoted above. Obsolete and abandoned assets had always been the subject of deduction from income under the practice and the decisions:

> "With knowledge, it must be assumed, of the established practice of the Bureau in this matter the Congress included in the deductions which might be here taken for depreciation or exhaustion, wear and tear 'a

reasonable allowance for obsolescence' (Secs. 214 (a) 8 and 234 (a) 7, Act of February 24, 1919). The language employed is significant, 'a reasonable allowance for exhaustion, wear and tear of property used in the trade or business, including a reasonable allowance for obsolescence.' This language signifies that it was not the intent to add a new kind of deduction but to permit the inclusion of a different element, to wit, 'obsolescence,' in exhaustion, wear and tear. No different method of computing the deduction for obsolescence than that theretofore used in the case of exhaustion, wear and tear was prescribed, and the presumption from the language employed in permitting this deduction clearly indicates that a different method was not contemplated.

"The existence of obsolescence under the earlier Acts was recognized but, as it was held not to be included in the terms 'depreciation' or 'exhaustion, wear and tear,' a deduction on account of obsolescence was only permitted when it had ripened into obsoleteness.

"As this resulted in throwing the total deduction for obsolescence as distinguished from depreciation into one year, it frequently happened that the then income was less than the allowable deduction and the cost or March 1, 1913, value was not fully returned to the taxpayer. To relieve in a measure this situation Congress provided for the recognition of obsolescence as a progressive process as distinguished from obsoleteness which was accomplished status, but, as clearly pointed out in Sol. Op. 114, there is nothing in the Act to indicate that Congress intended that this provision should have a retroactive effect."

Matter of Great Lakes Steamers, A. R. R., 963, C. B. I-1, June, 1922, p. 161 (Committee Appeals and Reviews).

The Commissioner could not lawfully reduce the statutory right from a deduction for obsolescence to a deduction for obsoleteness conditional upon abandonment. Only the Congress could make such a limitation and it might not

delegate the power to do so. To that extent the regulation is void.

International Railway Company v. Davidson, 257 U. S., 506, 66 L. Ed. 341.
U. S. v. George, 228 U. S., 14, 15 L. Ed. 712.
Williamson v. U. S., 204 U. S., 425, 52 L. Ed. 278.
U. S. vs. 200 Barrels of Whiskey, 95 U. S., 571, 24 L. Ed. 491.
Morill v. Jones, 106 U. S., 466, 27 L. Ed. 268.
Waite v. Macey, 246 U. S., 606, 62 L. Ed. 895.
Tracy v. Swartwout, 10 Peters, 80, 9 L. Ed. 354.

The various divisions of the Board of Tax Appeals have often allowed obsolescence deductions on account of the effect of prohibition on the tangible assets of breweries. In many cases the obsolescence deduction was permitted although the assets had not been abandoned.

Manhattan Brewing Company, 6 BTA, 952.
Multibestos Company, 6 BTA, 1060.
Corsicana Gas & Electric Company, 6 BTA, 565.
J. Chr. G. Hupfel, Inc., 9 BTA, 944.
Seas Shipping Company, Inc. v. Commissioner, 16 BTA, 841.

POINT III.

The taxpayer's conduct satisfied the requirement for abandonment of assets.

The taxpayer abandoned the brewing and sale of beer, October 29, 1919 (R. 31, 34). To preserve its machinery as well as to see if the new business could be made to pay (R. 27) it then manufactured a cereal beverage which did not resemble its prior product in power, in taste or in popularity, but did resemble it in appearance. Such a course did not vitiate the abandonment of the assets for the brewing of beer. The business was a different one and the product and its market were different.

If the Commissioner is right that it is necessary to close the plant and shut off the machinery from any available use to constitute abandonment, then the closing of one-third of the area of building No. 4 (R. 31), and the surrender of 84% of the use of the east half of building No. 3 (R. 32) were an abandonment in the strictest sense. The Board of Tax Appeals found the depreciated cost and value of these buildings at the beginning and end of the obsolescence period and on March 1st, 1913 (R. 31, 32). If the continuance of only a 16% use does not satisfy the regulation, then the regulation requires obsoleteness and not obsolescence because it takes no account of the gradual cessation of the use of the apparatus rapidly becoming obsolete.

We have already pointed to the findings (R. 28, 29) and to the stipulation, Appendix "A," establishing that the taxpayer well realized in 1917, 1918 and 1919 that its business was to be ended early in 1920. This was no conjecture as in the case of *Lassen Lumber & Box Co. v. Blair*, 27 F.

(2d) 17, cited by the Commissioner. The facts were notorious. The activities of the Executive, the Congress and the States first effective August 10, 1917, in war time prohibition reducing the alcoholic content to 2¾ by weight, are set forth in the complaint (R. 3, 4, 5) and uncontroverted by the answer (R. 22, §6). It is found that the assets of the taxpayer were reduced almost $200,000 in value during the years 1918 and 1919 by the certainty of prohibition (R. 32, 33). Another local brewery took a larger deduction for obsolescence than the taxpayer did and then sold its assets for a price which showed that the deduction was too small. The findings establish that the taxpayer has more than discharged its burden of proof upon this issue.

The Commissioner's position (p. 16) that the assets "were not obsolescent but were idle simply because of decreased volume of business" is an accounting distinction entitled to no weight in the construction of this statute enacted for the benefit of all taxpayers. If ever progress made an art obsolete the progress of prohibition effected that condition for brewing. (Opinion below, R. 50.)

POINT IV.

The undisputed loss in the value of taxpayer's assets is deductible as such if the obsolescence deduction is refused.

There are ample findings to show that a loss actually occurred in 1918 in the reduction of the value of taxpayer's assets by government intervention. The amount of the loss is undisputed and the reduction in value of the assets is clearly found. The assessment of a tax upon the income of taxpayer's business should properly take the loss into account. There could be no hope of recoupment of the loss even if the taxpayer were "an incorrigible optimist." The loss was a closed transaction when the Eighteenth Amendment was presented to the States and certainly when it was ratified.

This is not a case of contract liability as in the *Lewellyn* case and the *American Code Company* case cited by the Commissioner. It is an actual loss in the tax year.

> "The statute obviously does not contemplate, and the regulations * * * forbid the deduction of losses resulting from the mere fluctuation in value of property owned by the taxpayer (citing cases), but with equal certainty they do contemplate the deduction from gross income of losses which are fixed by identifiable events such as the sale of property * * * or caused by its destruction or physical injury * * * or in the case of debts by the occurrence of such events as prevent their collection * * *"
>
> *U. S. vs. White Dental Mfg. Co.*, 274 U. S., 398.

Any regulations which limit the right to use so obvious and complete a loss in computing taxpayer's income are beyond the power of the Commissioner and unlawful under the cases which we have cited under Point II of this brief.

The case of *Dick & Bros. Brewing Co. vs. U. S.*, cited by the Commissioner involves only good will, and, so far as the opinion shows, the questions here raised were not considered.

Conclusion.

The decree of the Circuit Court of Appeals for the Second Circuit should be affirmed and the Writ dismissed.

Respectfully submitted,

BASIL ROBILLARD,
Counsel for Respondents.

Appendix "A."

STIPULATION OF FACTS.

The following facts are hereby stipulated by and between the attorney for the Taxpayer and the counsel for the solicitor for the Commissioner of Internal Revenue:

1. The Niagara Falls Brewing Company, the Taxpayer, was duly organized and incorporated under and by virtue of the laws of the State of New York February 28th, 1902, and has and at all times hereinafter had its office and place of business in Niagara Falls, New York.

2. The business of the Taxpayer prior to September 5th, 1917, the date of the incidence of the Eighteenth Amendment to the Constitution of the United States, and the acts in enforcement thereof, was the manufacture, production, sale and distribution of a malt and spirituous liquor known as beer, containing more than one-half of one per cent alcohol by volume, and the business of Taxpayer and its good will were created and conducted by the manufacture and sale of such beverage.

3. The Taxpayer upon its organization purchased the buildings and equipment of the Niagara Falls Brewing Company, a joint stock association existing in Niagara Falls, New York, and assumed the current liabilities of said association.

4. The Taxpayer thereafter built some new buildings and purchased and installed some additional machinery, fixtures and equipment, which buildings, machinery, fixtures and equipment were specially constructed, designed and adapted to the Taxpayer's business of manufacturing

beer and were not readily adaptable to other uses. This property and equipment were devoted solely to the business of Taxpayer in making beer and "Pep" beer containing less than one-half of one per cent of alcohol by volume prior to the incidence of Wartime Prohibition and the Eighteenth Amendment and statutes in enforcement thereof.

5. On February 12th, 1918, the Board of Directors of Taxpayer, upon recommendation of the stockholders of Taxpayer's meeting held on the same day, authorized the Executive Committee to investigate and create a soft-drink plant of the Taxpayer, and on June 21st, 1918, directed the execution of a contract for the purchase of soft-drink manufacturing equipment, and on or about the 1st day of July, 1918, commenced the manufacture of soft-drinks.

6. Said selling of beer and malt and spirituous liquors was discontinued because of the incidence of the Eighteenth Amendment to the Constitution of the United States and the statutes in enforcement thereof, but the making and selling of soft-drinks continued after the incidence of such constitutional amendment and such statutes, and also the making and selling of beer of alcoholic content of less than one-half of one per cent (hereafter called dealcoholized beer).

7. No part of the obsolescence or extraordinary depreciation claimed by the Taxpayer, herein questioned, was computed upon or claimed on account of the depreciation of buildings, machinery and equipment for the manufacture of soft-drinks other than dealcoholized beer.

8. The investment in equipment for the manufacture of soft-drinks other than dealcoholized beer was as follows:

	Investment	*Depreciation*
1918	$5,033.09	$ 0
1919	8,175.98	553.31
1920	9,027.54	1,448.49
1921	9,200.79	1,448.49

9. The buildings, machinery and equipment for the manufacture of beer and malt and spirituous liquors were acquired for the most part prior to March 1st, 1913, and the cost, accrued depreciation, and the depreciated cost (hereinafter called "the figures") thereof on March 1st, 1913, were:

	Cost	*Accrued Dep'n*	*Depreciated Cost*
Land	$100,000.00	$ 0	$100,000.00
Buildings	196,667.97	48,475.79	148,192.18
Machinery	71,769.68	11,111.33	60,658.35
Casks and Tanks	27,643.00	6,668.54	20,974.46
Horses, Wagons, etc.	8,988.50	948.87	8,039.63
Office Furn. & Fx.	2,238.90	302.25	1,936.65
Auto Trucks	4,900.00	703.00	4,197.00
Signs	500.00	125.00	375.00
Small Cooperage	2,576.50	x	2,576.50
Saloon Furn. & Fx.	22,852.06	6,961.52	15,890.54
Outside Property	38,128.55	x	38,128.55
TOTALS	$476,265.16	$ 75,296.30	$400,968.86

10. At December 31st, 1917, the like figures thereof were:

	Cost	*Accrued Dep'n*	*Depreciated Cost.*
Land	$100,000.00	$ 0	$100,000.00

Buildings	229,999.32	80,851.25	149,148.07
Machinery	117,618.07	23,524.58	94,083.49
Casks and Tanks	40,399.35	7,855.76	32,543.59
Horses, Wagons, etc.	8,643.50	1,391.76	7,251.74
Office Furn. & Fx.	3,091.24	878.50	2,212.74
Auto Trucks	13,073.94	5,934.10	7,139.84
Small Cooperage	18,497.78	17,595.56	902.22
Saloon Furn. & Fx.	27,758.14	19,414.98	8,343.16
Outside Property	71,457.76	1,299.84	70,157.92
TOTALS	$630,539.10	$158,746.33	$471,792.77
Less Adjustment		7,219.36	7,219.36
NET	$630,539.10	$151,526.97	$479,012.13

In arriving at these figures the Commissioner restored to surplus at December 31st, 1917, all depreciation previously disallowed by him through an adjustment:

Dr.—Depreciation Reserve	$48,881.58	
Cr.—Surplus		$48,881.58

This adjustment erroneously included disallowed depreciation not reflected in the Depreciation Reserve, all on Outside Property, viz.:

Main & Niagara Streets	$5,000.00
Michigan Street	261.83
Miscellaneous property sold in 1917	1,957.53
TOTAL	$7,219.36

This depreciation had been credited direct to Outside Property Accounts. The adjustment should have been made as follows:

Dr.—Outside Property, Main & Niagara Sts.	$5,000.00	
Dr.—Outside Property, Michigan St.	261.83	
Dr.—Profit and Loss, 1917	1,957.53	
Cr.—Surplus		$7,219.36

The correction of this error requires the following adjustment:

Dr.—Outside Property, Main & Niagara Sts.	$5,000.00	
Dr.—Outside Property, Michigan St.	261.83	
Dr.—Surplus	1,957.53	
Cr.—Depreciation Reserve		$7,219.36

After this correction the figures as at December 31st, 1917, as determined by the Commissioner and accepted by the Taxpayer are:

	Cost	*Accrued Dep'n*	*Depreciated Cost*
Land	$100,000.00	$ 0	$100,000.00
Buildings	229,999.32	80,851.25	149,148.07
Machinery	117,618.07	23,524.58	94,093.49
Casks and Tanks	40,399.35	7,855.76	32,543.59
Horses, Wagons, etc.	8,643.50	1,391.76	7,251.74
Office Furn. & Fx.	3,091.24	878.50	2,212.74
Auto Trucks	13,073.94	5,934.10	7,139.84
Small Cooperage	18,497.78	17,595.56	902.22
Saloon Furn. & Fx.	27,758.14	19,414.98	8,343.16
Outside Property	76,719.59	1,299.84	75,419.75
TOTALS	$635,800.93	$158,746.33	$477,054.60

The item of Outside Property, Main and Niagara Streets, was sold in 1918, and the cost thereof used in computing the gain or loss on the sale thereof was taken without adding thereto the said item of $5,000.00 of cost written off directly and not restored thereto as outlined above.

11. The following action was taken at a meeting of the Executive Committee of the Directors of Taxpayer held June 27th, 1917, as duly recorded in the minutes thereof:

> "The committee here talked over in general the license question and other matters pertaining to the brewing industry including the pending legislation at Washington regarding the brewing of malted liquors and future prospects if laws were enacted restricting same.
>
> "The committee also made a thorough inspection of the brewery properties including the new bottling plant which is now running in first-class condition."

12. The following action was taken at a meeting of the Executive Committee of the Directors of Taxpayer held August 29th, 1917, as duly recorded in the minutes thereof:

> "The subject of manufacturing a temperance beer in the near future was brought up and discussed without any action being taken."

13. The following action was taken at a meeting of the Executive Committee of the Directors of Taxpayer held September 5th, 1917, as duly recorded in the minutes thereof:

> "On motion duly seconded and unanimously carried it was decided to have Brewmaster Daegelow make a brew of what is generally known as Temperance Beer and have it in readiness for sale by October 1st, if possible so that some of the customers who were not granted a license could continue in business.
>
> "On motion, duly seconded and unanimously carried, the President was authorized to have special bot-

tles and labels made to use on the new product and to use his best efforts to have same here previous to Oct. 1st."

14. The following action was taken at a meeting of the Executive Committee of the Directors of Taxpayer held November 2nd, 1917, as duly recorded in the minutes thereof:

"The President informed the committee that he had met Mr. Schultz the Buffalo Brewery Architect and discussed with him the cost and details of a soft drink bottling establishment, and that a report of his findings would be submitted at a later date.

"At the suggestion of Mr. Nye, the committee here sampled the new temperance beverage 'Pep' and after drinking several glasses pronounced it very good and a correct imitation of beer without the alcohol. Mr. Nye informed the committee that the new drink would in all probability be placed on the market just previous to Thanksgiving."

15. The following action was taken at a meeting of the Executive Committee of the Directors of Taxpayer held November 23rd, 1917, as duly recorded in the minutes thereof:

"The President stated to the committee that all was in readiness to place 'Pep' on the market and that the sale of same would commence on the 28th day of November, and that he would like the committee to fix a price for bottled and in the wood.

"On motion, duly seconded and unanimously carried, the price of 'Pep' in wood was fixed at $8.00 per barrel and in bottles at $1.20 per case or 60 cents per half case.

"The President reported to the committee that he had visited the Ballantine Brewing Company's Soft Drink concern at Newark, N. J., and that he found the operation of bottling temperance drinks very simple and profitable. He further stated that he called upon Mr. Hires of the Hires Root Beer Company in New

York City who explained the root beer proposition in detail and that Mr. Hires was very anxious to have this company handle the product in a three county territory.

"On motion, duly seconded and unanimously carried, the President's report was received and filed."

16. At a regular meeting of the Board of Directors of Taxpayer held November 13th, 1917, action was taken, as in the minutes of said meeting recorded, as follows:

"On motion of Mr. Krull, seconded by Mr. Mayle, and unanimously carried, the Executive Committee were instructed to investigate the kind and cost of necessary machinery for manufacturing and bottling Hires Root Beer and other temperance beverages, and also to investigate other breweries manufacturing and bottling temperance beverages, and if they deem it advisable to proceed therewith, they be authorized to so proceed and conserve the interests of the brewing company and that they be further authorized to enter into any and all contracts necessary for such purpose."

17. The following action was taken at a meeting of the Executive Committee of the Directors of Taxpayer held November 28th, 1917, as duly recorded in the minutes thereof:

"The matter of manufacturing a line of soft drinks was thoroughly discussed and Mr. Nye informed the committee that he had been investigating the proposition to some extent and would be in a position to give some definite information on the subject very shortly.

"On motion, duly seconded and unanimously carried, the President was authorized to visit New York and Newark, N. J., in the interest of manufacturing soft drinks. * * *

"The committee here made an inspection of the premises with a view to locating a soft drink manufacturing and bottling plant."

18. The following action was taken at a meeting of the Executive Committee of the Directors of Taxpayer held December 12th, 1917, as duly recorded in the minutes thereof:

> "The President submitted a communication from the Charles E. Hires Company stating that they would like very much to have the company take action on their soft drink proposition and that they were very anxious to have the Hires Syrup in Niagara Falls at the earliest possible moment as the transportation situation looked rather dark according to reports.
>
> "On motion, duly seconded and unanimously carried, the communication was received and filed.
>
> "The President presented a letter from the United States Brewers Association calling the attention of brewers to the new law in effect January 1st, governing the manufacture of malted products.
>
> "On motion, duly seconded the communication was ordered received and filed.
>
> "A communication from Mr. C. W. Feigenspan, President of the United States Brewers Association was read, in which was stated that he expected every brewer in the United States to put forth their best efforts to fight against the proposed prohibition legislation to be enacted by the 48 states in the Union for National Prohibition.
>
> "On motion, duly seconded, the communication was ordered received and filed and the Secretary instructed to write Mr. Feigenspan to the effect that this company had faith in the cause and in him and that he had our assurance of unswerving support."

19. The following action was taken at a meeting of the Executive Committee of the Directors of Taxpayer held February 8th, 1918, as duly recorded in the minutes thereof:

> "Mr. Cohn was present and conferred with the committee and Mr. Ashton, the auditor with respect to the annual report and the matter of taxation and the amount of depreciation to be written off on buildings, machinery, etc.

"Other matters of a financial nature were brought up and discussed at some length after which an inspection of the plant and machinery was made."

20. At the annual meeting of the Stockholders of the Taxpayer held February 12th, 1918, the following action was taken, as duly recorded in the minutes thereof:

"The President of the company made a report as to the condition of the brewing business generally and as to the growing tendency of prohibition. The questions so raised by the President were discussed by the stockholders, and on motion seconded and unanimously carried, it was resolved that it is the sense of this meeting that the officers, directors and members of the Executive Committee make such investigation and take such action in respect to the installation of a plant for the manufacturing of all kinds of soft drinks as in their judgment might be necessary for the interests of this company and for the preservation of its business, and that the stockholders recommend to them the taking of such action and making of all the necessary expenditures, if in their judgment it is advisable to carry the same into effect."

21. At a regular meeting of the Board of Directors of Taxpayer held February 12th, 1918, action was taken, as in the minutes of said meeting recorded, as follows:

"The recommendation of the stockholders of the company at the meeting this day held, in respect of the investigation and installation of the soft drink proposition was discussed, and on motion seconded and unanimously carried, the Executive Committee was authorized and empowered to cause such investigation to be made, and if in their judgment it was advisable so to do, from time to time to make the necessary expenditures for the installation of a soft drink plant, upon such terms and through such medium as in their judgment it is advisable so to do."

22. The following action was taken at a meeting of the Executive Committee of the Directors of Taxpayer held

March 22nd, 1918, as duly recorded in the minutes thereof:

"The President submitted a communication from the Food Conservation Committee at Washington to the effect that beginning April 1st, 1918, only 70% of the production of April, May and June could be produced during the corresponding three months of the present year.

"On motion, same was ordered received and filed and the brewmaster instructed to observe the instructions contained therein."

23. The following action was taken at a meeting of the Executive Committee of the Directors of Taxpayer held April 22nd, 1918, as duly recorded in the the minutes thereof:

"The President submitted a proposal from Jacob House & Sons of Buffalo, N. Y., in which they agreed to furnish for use in equipping the new soft drink bottling plant, the following:

"One Big Buffalo Carbonator, capacity 250 to 300 gallons per hour, including double drum high pressure gas outfit, and ¾" block tin pipe not over eight feet in length, to connect with Crown Junior Machine, f. o. b. Niagara Falls..... $380.00

"One—No. 5 Lynn Filter complete, f. o. b. Niagara Falls, N. Y..... 235.00

"Two—Syrup Percolaters with capacity each of forty gallons filtered syrup, $32.50 each 65.00

"Two—40 gallon self drained style, stone syrup jars, $15.00 each..... 30.00

"Straight tinned outlet faucets for same, each $1.00.

"All f. o. b. Niagara Falls.

"On motion, duly seconded and unanimously carried, the President was authorized to enter into contract with Jacob House & Sons for the equipment above mentioned at the price stated.

"The President submitted a proposal from the Crown Cork & Seal Company, in which they agreed to furnish one Junior Automatic Crown Soda Machine, f. o. b. Baltimore for the sum of $1634.00.

"On motion, duly seconded and unanimously carried, the President was authorized to execute a contract with the Crown Cork & Seal Company to furnish the machine above mentioned for the sum of $1634.00."

24. By action of the Board of Directors of Taxpayer duly taken at a meeting held May 24th, 1918, as recorded in the minutes thereof, said Executive Committee was discontinued on and after June 1st, 1918, and at said meeting the following action was taken as duly recorded in the minutes thereof:

"A discussion was here had as to the advisability of this company engaging in the so-called soft drink or beverage business, and on motion of Mr. Schoellkopf, seconded by Mr. Mayle, the President of this company was authorized to negotiate with A. C. Frier of Niagara Falls, N. Y., who is engaged in the business of manufacturing, bottling and vending so-called soft drinks, to see if this company could acquire the business conducted by him, and at the same time secure his services as Superintendent of the soft drink plant."

25. At a meeting of the Board of Directors of Taxpayer held September 2nd, 1918, action was taken, as in the minutes of said meeting recorded, as follows:

"A discussion was here had as to the further continuance of the business of this company, the likelihood of prohibition, and its effect upon the property, assets and good will of the company, and the future course of the company in respect to its property and business in the event of prohibition becoming a fact.

"On motion of Mr. Schoellkopf, duly seconded by Mr. Chormann, the President was authorized and requested to appoint a committee of three for the purpose of considering the future of the company and a reorganization thereof, the President to file a list of such committee with the Secretary."

26. At a meeting of the Board of Directors of Taxpayer held November 26th, 1918, action was taken, as in the minutes of said meeting recorded, as follows:

"The President made a verbal report on the conditions relating to the brewing business in general, and stated that pursuant to the resolution adopted at the meeting September 2, 1918, directing him to appoint a committee of three for the purpose of considering the future of the company and the re-organization thereof, he had appointed Messrs. Paul A. Schoellkopf, Frederick Chormann and Rudolph V. Rose as such committee. * * * *

"On motion of Mr. Chormann, seconded by Mr. Rose, the President and auditor of this company were authorized to investigate and make a report on the question of lawful depreciation of plant, property and equipment of this company, and to make such depreciation as in their judgment, after careful investigation, is just, lawful and proper."

27. At a meeting of the Board of Directors of Taxpayer held February 5th, 1919, action was taken, as in the minutes of said meeting recorded, as follows:

"On motion of Mr. Krull, seconded by Mr. Mayle, and unanimously carried, the following resolution was adopted:

"WHEREAS, the Accounting Department of this company has after due consideration and consultation with the officers of the company, and with its counsel, made up an operating statement for the year 1918, in which charges have been made for extraordinary depreciation to that part of the plant of this company which has been acquired for and is peculiarly adapted to the use in the brewing of malt liquors, because of actual as well as obvious and impending conditions tending to render such portion of the plant of greatly decreased value, because of conditions arising during said year 1918; and

"WHEREAS, this Board has duly considered the charges to operation so made, as shown by the report submitted on this date,

"NOW, THEREFORE, BE IT RESOLVED, that the action of the accounting officers in making such charges to operations for depreciation of the tangible

property of this company, occurring through actual as well as obvious and impending conditions relating to the business of the company for the year 1918, be and the same is in all things ratified and approved, and the Accounting Department is hereby instructed permanently to enter such charges for extraordinary depreciation for the year 1918, amounting to $110,147.52, as tentatively proposed, upon the operating statement submitted to this Board."

28. At the annual meeting of the Stockholders of the Taxpayer held February 11th, 1919, the following action was taken, as duly recorded in the minutes thereof:

"On motion seconded and unanimously carried it was RESOLVED, that all acts, things and transactions of the officers, directors and members of the Executive Committee of this company, since the date of the last annual meeting to the day of the date of this meeting, including the execution and delivery of all documents, contracts, notes, papers and writings signed by them or any of them, or entered into for and on behalf of this company, as well as all salaries, disbursements and other payments of every kind and character made during such year, be and each of them is hereby specifically in all things ratified, confirmed and approved, with the same force and effect as if each and every of such acts, things and transactions had been done and performed or made upon the express instructions and directions of the stockholders in respect thereto. * * * *

"A general discussion was here had as to the condition of the business, generally, and as to the probable losses which the company might have to sustain during the year through prohibition movement, if the same became effective. The President asked for suggestions from the stockholders as to the business and affairs of the company, offered to furnish any information which any of them might request. No such request being made, or explanations desired, and there being no further business to come before the meeting, the same was, on motion, seconded and unanimously carried, adjourned."

29. The charges against earnings of the year 1918 re depreciation and obsolescence made on the books and records of the Taxpayer in determining its income as recorded and as returned to the Federal Government as the basis of determining its income and profits tax liability for that year were:

	Regular Depreciation	*Obsolescence*
Buildings	$ 4,597.63	$ 27,014.33
Machinery	5,389.93	59,430.22
Casks and Tanks	2,019.81	16,912.87
Horses, Wagons, etc	862.98	1,268.56
Office Furn. and Fx.	152.48	532.42
Autos and Trucks	2,611.26	2,204.40
Small Cooperage	650.00	2,132.71
Saloon Furn. and Fx.	833.21	522.01
Total	$17,117.30	$110,047.52

30. The like charges for the year 1919 were:

	Regular Depreciation	*Obsolescence*
Buildings	$ 5,049.28	$ 40,000.00
Machinery	5,854.02	10,000.00
Casks and Tanks	2,071.52	928.48
Office Furn. and Fx.	157.89	114.24
Auto Trucks	100.00	0
Small Cooperage	400.00	0
Saloon Furn. and Fx.	0	450.00
Outside Property	0	5,647.27
Total	$13,632.71	$ 57,139.99

31. After sundry examinations, hearings, etc., the Commissioner computed the income and profits taxes of this corporation to be:

1918	—	$ 20,975.05
1919	—	5,152.57
		$ 26,127.82

whereas the said taxes as determined by the Taxpayer were:

1918	—	$ None
1919	—	138.92
		$ 138.92

the net differences being:

1918	—	$ 20,975.05
1919	—	5,013.65
		$ 25,988.70

which the said Commissioner formally determined and assessed as such under date of November 26th, 1924, assessing same under the provisions of Section 274 (d) of the Revenue Act of 1924.

32. Notices and demand for payment of said additional assessments were thereafter received. Claim in abatement thereof, accompanied by bond, was filed on January 15th, 1925, which claim was rejected under date of August 13th, 1925, and petition to this Board duly filed.

33. In his determination of additional taxes due the Commissioner has readjusted depreciation, obsolescence, and losses as originally taken by the Taxpayer as follows:

1918	*Claimed on Original Return*	*Allowed by Commissioner*		*Difference*
Regular Depn.	$ 17,117.30	$20,552.05		3,434.75
Obsolescence	110,047.52	0	*(minus)*	*110,047.52*
Loss, Casks & Tanks	0	18,210.16		18,210.16
	127,164.82	$38,762.21	*(minus)*	*$88,402.61*
1919				
Regular Depn.	$ 13,632.71	$20,983.05		$ 7,350.34
Obsolescence	57,139.99	0	*(minus)*	*57,139.99*
	$70,772.70	$20,983.05	*(minus)*	*$49,789.65*

34. The book cost and the net depreciated book cost of the fixed assets of the Taxpayer at December 31st, 1918, and 1919 were:

	Dec. 31, 1918		*Dec. 31, 1919*	
	Book Cost	*Net Dep't'd Cost*	*Book Cost: Net*	*Dep't'd Cost*
Land	$100,000.00	$100,000.00	$100,000.00	$100,000.00
Buildings	229,999.32	108,057.31	229,999.32	63,088.03
Machinery				
Beer	131,675.21	32,500.00	134,542.63	19,966.71
Soft-drink	4,533.09	4,533.09	7,400.18	6,946.87
Casks & Tanks	40,399.35	5,000.00	40,399.35	2,000.00
Horses, Wagons, etc.	8,638.50	1,000.00	8,570.50	932.00
Office Furn. & Fx.	3,101.74	600.00	3,173.87	400.00
Auto Trucks				
Beer	15,283.85	3,000.00	15,568.60	3,284.75
Soft-drinks	500.00	500.00	775.80	675.80
Small Cooperage	2,632.71	500.00	2,232.71	100.00
Saloon Furn. & Fx.	28,383.06	100.00	28,733.06	0
Outside Property	38,128.55	38,128.55	38,147.27	32,500.00
TOTALS	$603,275.38	$293,918.95	$609,543.29	$229,814.16

34. The sales of the products of this company in the years 1912-1921, inclusive, were:

	Barrels		
		Cereal	
	Beer	*Beverage*	*Soft-drinks*
1912	33,177		
1913	37,581		
1914	32,756		
1915	30,681		
1916	38,388		
1917	37,196	16	
1918	30,204	327	$6,092.35
1919	17,823	8	22,451.35
1920	0	7,921	21,507.43
1921	0	2,852	

The sale of beer was discontinued October 29th, 1919.
The first sale of cereal beverage (dealcoholized beer) was November 27th, 1917, under the name of "Pep."
The first sale of soft-drinks was July 1st, 1918.

35. The Taxpayer under date of January 15th, 1922, leased all of its buildings, plant and equipment, including its soft-drink equipment, under a lease running for a period of three months, renewable at three month intervals at the option of the lessee, and which lease is still in operation, at an annual rental of $5,000.00 plus taxes, insurance and repairs.

36. The assessed valuation of the real property of the Taxpayer was, by action of the Assessor of the City of Niagara Falls, New York, reduced from $223,460.00 to $183,460.00 in 1918, and was further reduced in 1923 to $104,760.00.

37. The Taxpayer has duly dissolved under voluntary consent of its stockholders by certificate to such effect filed with the Secretary of State of the State of New York on December 1st, 1921, its affairs in dissolution being administered by its directors as Trustees in Dissolution pursuant to Section 220 of the General Corporation Law (now Section 105 of the Stock Corporation Law) of the State of New York.

Dated: March , 1927.

NIAGARA FALLS BREWING COMPANY,
By BASIL ROBILLARD,
Attorney.

COMMISSIONER OF INTERNAL REVENUE,
By A. W. GREGG,
Solicitor.

SUPREME COURT OF THE UNITED STATES.

No. 61.—October Term, 1930.

David Burnet, Commissioner of Internal Revenue, Petitioner, *vs.* Niagara Falls Brewing Company and Paul A. Schoellkopf, Charles E. Haeberle, et al., etc.	On Writ of Certiorari to the United States Circuit Court of Appeals for the Second Circuit.

[February 24, 1931.]

Mr. Justice Butler delivered the opinion of the Court.

In making its tax returns for 1918 and 1919 the brewing company, because of approaching prohibition, made deductions for obsolescence of its buildings, machinery and equipment. The Commissioner disallowed the deductions on the ground that after prohibition the taxpayer continued to use his property to make and sell near beer and other non-intoxicating beverages. The Board of Tax Appeals sustained the Commissioner. 13 B. T. A. 1040. The Circuit Court of Appeals reversed. 38 F. (2d) 217.

The pertinent words of the statute, Revenue Act of 1918, § 234 (a) (7) are: "A reasonable allowance for the exhaustion, wear and tear of property used in the trade or business, including a reasonable allowance for obsolescence."

The Government contends that this statute did not authorize a deduction for obsolescence of tangible property resulting from the imminence of prohibition. But in the *Gambrinus* case just decided we hold the contrary.

The Government also maintains that on the facts of this case no allowance for obsolescence should be made.

We take judicial notice of the following. Prior to the submission of the Eighteenth Amendment in 1917, more than 30 States had enacted prohibitory laws. A war measure, effective August 10, 1917, required the reduction of the alcoholic content of beer. The proposed amendment was ratified by 12 States in the first six months

of 1918 and by three more before the expiration of that year; 21 States ratified in the early part of January, 1919, and in that month the Amendment became a part of the Constitution and took effect one year later, January 16, 1920.

There is no controvery as to facts found by the Board of Tax Appeals:

The brewing company from 1902 until October, 1919, was engaged in making and selling beer. Its sales from 1912 to 1917 inclusive ranged from 30,681 to 37,176 barrels per year. Due to war-time prohibition, its sales fell off in 1918 to 30,204 barrels, about 19 per cent. less than the sales of the preceding year, and in 1919 to 17,823 barrels, about 40 per cent. less than in 1918.

At the end of 1917 the depreciated cost, and actual value, of the company's land, buildings and equipment was $477,054.60. After deducting the allowances in 1918 and in 1919 for exhaustion, wear and tear of its plant and for obsolescence of property used for making beer, the book value of such property was reduced to $279,117.08. But due to prohibition laws its actual value at the end of 1919 was only $90,475. That is $188,642.08 less than the book value after such deductions.

Its buildings, machinery and equipment were designed and constructed for the brewing and selling of beer and were not available or readily adaptable to other uses. The buildings were damp, the floor levels uneven; there were few openings for light and no elevators, and the property was located in a manufacturing zone. Much of the machinery could not be removed without dismantling or tearing out the walls of the building and some of it could not be removed except by tearing out a side of the building. The company's officers considered selling or converting its buildings and machinery into a plant for a dairy, cold storage, ice cream manufacturing, dry storage, ice manufacture, fruit storage, semicold storage, machine shop, or chemical plant. They could find no use for the property except for the purpose of making near beer and other soft drinks.

In 1917 the company began to manufacture near beer and for that purpose used the machinery and processes employed in the making of beer. An additional process for dealcoholizing was necessary. It sold 16 barrels in that year, 327 in 1918, 8 in 1919, 7,921 in 1920 and 2,852 in 1921.

In 1918 it began the manufacture of other soft drinks by use of machinery not here involved. In October, 1919, because of prohibition, the company discontinued the making of beer. It abandoned the lower floor of one of its buildings which had been devoted to storing and aging beer. That process is not involved in making near beer. Thereafter a part of another building with the equipment therein which had been used three or four times a week in making and bottling beer was used only once in about two weeks in making near beer. Apparently the rest of the property was used in connection with the making of such near beer and other soft drinks as were made by the company prior to its going out of business.

The company could not operate at a profit after prohibition and the corporation was voluntarily dissolved in December of 1921. Its affairs were administered by its former directors acting as trustees. In January, 1922, they leased all the property, including equipment that had been added for the making of soft drinks, for a term of three months with privilege of renewal by the lessee. The lease was still in effect at the time of the hearing before the Board in 1927. The rent was at the rate of $5,000 per year plus taxes, insurance and repairs.

The difference between the depreciated cost (found to be actual value) December 31, 1917, and the value of the property in 1918 and 1919 was due to the imminence and incidence of war-time and permanent prohibition. There was no material change in the value of land and buildings in the vicinity used for purposes other than brewing. In December, 1921, the company sold certain of its land, free from buildings, for $20,000. Up to the time of the hearing the highest offer for the remaining property that the company was able to secure was $35,000.

The Government argues that obsolescence is the state of becoming obsolete, that property is obsolete when it is no longer useful for the purpose for which it was acquired and cannot be used for any other purpose and that obsolescence begins only when there is a reasonable certainty that the property will become obsolete. And further, that there is no finding that at any time during the taxable years in question it became apparent that the property would become obsolete and that no inference to that effect can properly be drawn from the facts found.

In the solution of the problem here presented, no general or comprehensive definition of "obsolescence" is necessary. The word is much used and its meaning depends upon and varies with the connections in which it is employed. It has been said to be "the condition or process by which units gradually cease to be useful or profitable as a part of the property, on account of changed conditions."* Obsolescence is not necessarily confined to particular elements or parts of a plant; the whole may become obsolete. Obsolescence may arise as the result of laws regulating or forbidding the particular use of the property as well as from changes in the art, the shifting of business centers, loss of trade, inadequacy or other causes.

We are here concerned with the meaning of obsolescence as used in the above quoted clause of the taxing Act. Clearly the statute contemplates that, where warranted by the facts, the taxpayer shall have the benefit of, and in making his return may deduct in each year, a reasonable allowance to cover obsolescence of the tangible property. And that is in accord with sound principles of accounting. Cf. *Kansas City So. Ry.* v. *United States*, 231 U. S. 423, 451. *Pacific Gas Co.* v. *San Francisco*, 265 U. S. 403, 415. The provision is general and applied alike to all taxpayers; its purpose is to guide the ascertainment of taxable income in each year. It is a familiar rule that tax laws are to be liberally construed in favor of taxpayers. *Farmers Loan Co.* v. *Minnesota*, 280 U. S. 204, 212. *Bowers* v. *N. Y. & Albany Co.*, 273 U. S. 346, 350. *United States* v. *Merriam*, 263 U. S. 179, 188. *Shwab* v. *Doyle*, 258 U. S. 529, 536. *Eidman* v. *Martinez*, 184 U. S. 578, 583.

It would be unreasonable and violate that canon of construction to put upon the taxpayer the burden of proving to a reasonable certainty the existence and amount of obsolescence. Such weight of evidence as would reasonably support a verdict for a plaintiff in an ordinary action for the recovery of money fairly may be deemed sufficient. Neither the cost of obsolescence nor of accruing exhaustion, wear and tear that is properly chargeable in any period of time can be measured accurately. A reasonable approximation of the amount that fairly may be included in the accounts of any year is all that is required. In determining the proper deduction for obsolescence there is to be taken into consideration the amount

*Transactions, Am. Soc. C. E., Vol. 81, p. 1527.

probably recoverable, at the end of its service, by putting the property to another use or by selling it as scrap or otherwise. There is no hard and fast rule, as suggested by the Government, that a taxpayer must show that his property will be scrapped or cease to be used or useful for any purpose, before any allowance may be made for obsolescence.

There is no claim that, if allowable at all, the amounts deducted were excessive or that they were not properly allocated as between the two years in question. The rapid advance toward prohibition prior to and in 1917 was sufficient to warn one engaged in brewing beer that his business would probably be brought to an end at an early date. In January, 1919, before the tax return for 1918 was due, prohibition was established to take effect one year later. The facts found show that in the early part of 1918 the company was abundantly justified in concluding that upon the taking effect of prohibition it must cease to use its brewery for making beer.

It was then warranted in concluding that the period of obsolescence commenced about the first of 1918 and would end upon the taking effect of prohibition. The fact that prohibition would put all the breweries out of business is enough to show that it would be practically impossible to sell such properties or find other uses to which they profitably could be put. Due to prohibition the diminution in value of the company's property in 1918 and 1919 was about twice as much as the total of all sums deducted to cover obsolescence in those years. In that period over 80 per cent. of the 1917 value of its lands, buildings and equipment disappeared. Notwithstanding diligent efforts, the property could not be put to any profitable use or sold for more than a fraction of its value in 1917. The rents realized under a short term lease renewed from time to time for more than five years amounted to less than one and one-half per cent. of such value.

The facts found clearly show that obsolescence commenced about the beginning of 1918 and that the property became obsolete upon the taking effect of prohibition in January, 1920. The company was unable to find any profitable use to which the property could be put. The sums received on the sale and as rents constituted mere salvage.

Judgment affirmed.